Establishing a real estate giant

A case study on the growth journey of Samhällsbyggnadsbolaget i Norden AB (“SBB”) and the acquisition of Hemfosa Fastigheter AB (“Hemfosa”)

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ABSTRACT

This single-case study contains a two-track investigation of SBB, including the company’s growth journey and acquisition of Hemfosa. The aim is to display an in-depth analysis from a unique real estate narrative, social infrastructure, that provides key success factors and decisive insights from the remarkable growth journey as well as the all-time largest real estate M&A deal in the Nordics. First, with regards to SBB’s growth strategy, we identify non-cash acquisitions and a wide financing base with strong credit rating focus as fundamental in scaling the business. Although those strategy cornerstones have paved the way for rapid growth, we find that favorable market conditions with low interest rates has been a decisive factor, facilitating SBB’s ability to grow. Second, the Hemfosa transaction evolves around several key motives. Building scale by combining the two property portfolios and substantial synergies mainly from refinancing of Hemfosa’s bank debt in the bond market, thus exploiting SBB’s investment grade credit rating. In addition, we also find strong vertical integration motives and that Hemfosa was likely undervalued at the time of the transaction. The case further presents a Mix & Match bid composition as crucial to finance the deal and in parallel to safeguard the combined entity’s capital structure and credit rating, essential for realizing financial synergies and to maintain the ability to grow. In summary, the study sheds light on how real estate and the case aligns and differs from traditional theories in Finance.

Keywords: Real estate, M&A, growth, social infrastructure, non-cash acquisitions

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1. Introduction

On September 15th, 2019, the Sweden-based real estate company, Samhällsbyggnadsbolaget i Norden AB ("SBB"), announced the SEK 23.5bn takeover offer for all outstanding shares in Hemfosa Fastigheter AB ("Hemfosa"), a deal that would become the all-time largest real estate transaction in the Nordics (Fastighetsvärlden, 2019c). Founded in 2016, SBB had in short time accomplished astounding growth by building a SEK 30bn portfolio of properties in the Nordics, specialized towards residential properties and the recently established real estate segment in social infrastructure. Consequently, SBB had been recognized in the market for its intense growth strategy and was expected to continue growing through acquisitions. However, when announcing the intended public takeover of Hemfosa, the market was surprised that SBB already had the ability to consider acquiring a significantly larger company in such price range. The deal eventually turned out to be the largest M&A transaction in the Nordics in 2019 (Börskollen, 2020), creating the fourth largest Nordic real estate company with over SEK 70bn worth of properties in the portfolio. As a spectator, this raises question marks on how SBB managed to grow and carry out such a transaction. Therefore, we chose to conduct this case study which outlines the following research questions, in order to carefully display the growth journey and the Hemfosa transaction:

(1) How did SBB manage to achieve substantial growth in short time?

The study concludes that the cornerstones of SBB's business model have paved the way for growth. First, we find non-cash acquisitions paramount to achieve fast and sustainable growth since it has enabled SBB to scale the business model and simultaneously improve the equity ratio in the process. Secondly, we identify SBB's financing strategy, based on credit rating and a wide financing base, as crucial to build scale and as a result lower the cost of debt. Finally, the platform of key employees has been decisive for the practical implementation of the business model. In addition to the carefully outlined strategy, we further acknowledge that SBB has benefitted from favorable market timing and argue that it would have been nearly impossible to achieve similar growth in a high interest rate environment.

(2) Which were the main motives for acquiring Hemfosa and how did SBB finance the deal?

Most importantly, the deal would diversify and more than double SBB's property portfolio, establishing SBB as one of the largest Nordic real estate companies. In addition, it was set to generate substantial synergies, mainly financial due to differing capital structures and financing costs, from refinancing the Hemfosa loan book in the bond market at lower cost of debt, exploiting SBB's investment grade credit rating. On top that, SBB possessed detailed knowledge of unrealized values in the Hemfosa portfolio, pointing towards undervaluation and timing as key motives behind the deal. Further, we also identify vertical merger motives since the deal would complete weaknesses in the individual companies, by combining Hemfosa's property management organization and SBB's property development franchise. Finally, we find that the Mix & Match bid composition enabled SBB to finance the deal while safeguarding the combined entity's capital structure to maintain an investment grade credit rating post-deal.

1.1 Purpose

This thesis is written upon three purposes. In first instance with the objective to understand growth in a unique real estate narrative, focusing on fundamental drivers and key success factors through an investigation of SBB's growth journey. Secondly, the goal is to examine real estate M&A through an in-depth study of SBB's acquisition of Hemfosa. Lastly, the study intends to provide the Department of Finance at the Stockholm School of Economics with material that could be used to develop a case for teaching purposes.

1.2 Contribution

Although previous research exhaustively covers theories on company growth and plenty of M&A aspects, we find several touchpoints in the case study which contributes to existing research. First, on a fundamental level, we put emphasis on motives behind the deal, contributing to research which tends to focus more on the outcome of mergers and acquisitions (Trautwein, 1990). Secondly, the case study adds an in-depth display of a distinctive growth journey as well as a corporate transaction in the recently established real estate segment within social infrastructure. Thirdly, the case presents evidence that SBB has pursued non-cash acquisitions during its growth journey although their shares likely have been undervalued in the process, which contradicts with existing theory (Shleifer and Vishny, 2003; Dong et al. 2006) stating that non-cash acquisitions primarily are driven by overvaluation. Finally, we provide an example of real estate specific valuation, which in many differs significantly in comparison to conventional valuation models in finance such as FCF, for instance excluding consideration of earnings quality and growth capacity.

1.3 Outline

The thesis is structured as follows. Chapter 2 summarizes relevant existing research around growth, both conventional and real estate specific M&A theory and deal financing. Chapter 3 describes the applied research methodology to answer the research questions, including the data collection process and assessment of the research quality. Chapter 4 provides essential background information about the real estate market and relevant segments for the study. Chapter 5 introduces the investigated companies, SBB and Hemfosa, with focus on the business models, growth journeys and standpoints before the transaction. Chapter 6 features the case around SBB's acquisition of Hemfosa as well as how SBB prepared for and managed the deal. Chapter 7 contains analyses around the growth journey and the transaction in relation to existing theory, including an authors' standalone valuation of Hemfosa and transaction-related synergies. Lastly, Chapter 8 concludes this case study thesis by providing answers to the mentioned research questions.

2. Literature review

This chapter outlines a sample of previous research and academic findings on company growth and M&A in general, followed by M&A in a real estate context and M&A financing. Finally, the section presents government theory regarding privatization.

2.1 Company growth

Organizations looking for growth have three possible paths – *organic growth*, *M&A* and *joint ventures*. In terms of priority, theory suggests that organic growth should be the main focus and that businesses should consider M&A and joint ventures based on their skillsets, cash flow and targets. Further, M&A is a common strategy in mature marketplaces to consolidate the market by buying competitors, removing overlaps to create cost synergies (Davis, 2012). Harrison (1987) argues that most mergers fail to meet management expectations and can, in fact, create more problems than they solve, proposing joint ventures and international expansion as alternative means to achieve growth. These strategies tend to involve lower costs, require less risk-taking and cause less organizational upheaval than mergers. On the contrary, Shleifer and Vishny (2003) present an advantage of making acquisitions, which aside from perceived synergies, contribute to earnings growth and thereby help justify high valuations. Whittington et al. (2020) add to the point around acquisitions and argue that it enables companies to acquire proven businesses instead of spending resources on R&D to achieve comparable organic growth.

A common conception is that private firms seeking access to capital for expansion and growth, look towards a stock market listing. In theory, there are several arguments on why firms decide to list on a stock exchange. For instance, credibility with customers and suppliers, greater access to capital and the possibility to use company shares as currency for acquisitions and compensation. However, empirical evidence on the motives and investment activities of IPO firms are limited (Celikyurt et al., 2010). Kim and Weisbach (2008) examine motives for public equity offerings by estimating the uses of raised capital. The authors find that financing of capital expenditures and R&D as well as benefiting from overvaluation are the main motives for going public, especially in high market-to-book value firms. Celikyurt et al. (2010) examine the role of newly listed firms in M&A activity, finding that recently listed companies tend to have high acquisition appetites and show that IPOs significantly change the ability of firms to conduct acquisitions. Thus, suggesting that the ability to pursue acquisitions might be an important motive for an IPO. Brenner and Schroff (2004) look at the pros and cons of going public through an IPO versus the alternative route of a reverse merger, finding that reverse mergers are faster and less costly since the process can be completed in 45 days, instead of a year or more required for an IPO. Savings from a reverse merger mainly involve avoidance of extensive fees and the often-overlooked effect of distracting management from their normal duties. However, traditional IPOs offer better possibilities for owners to exit and exploit favorable market sentiment. Also, reverse mergers have been surrounded by controversy stemming from companies being able to avoid parts of the rigorous IPO process, putting the governance and earnings quality into question (Brenner and Schroff, 2004).

2.2 Mergers and acquisitions

Organizations are likely to at some stage of a life cycle go through a process of integration or separation. In general terms, change is a multilateral concept and has several underlying motives. The need for change can thus originate from various reasons such as growth ambitions or lack of efficiency (Davis, 2012). With emphasis on integration and the growth motive, M&A in several forms is a crucial component. M&A is an important, large and often complex investment for a company and involves decisions on how to engage, finance and pay for a M&A deal (Baker and Martin, 2011). Since for-profit organizations' ultimate objective is to maximize profits and shareholder wealth, plenty of techniques are used to achieve profit maximization, especially in fast-growing markets. For instance, M&A enables a company to enter new markets, launch new products and increase its portfolio (Malik et al., 2014).

In terms of history, Lipton (2006) shows that M&A activity started in the U.S. already during the late nineteenth century. Since then, M&A has been cyclical and occurred in clustered 10-15-year periods over the last century, in so-called merger waves (Whittington et al., 2020). Each merger wave has historically been characterized by a type of merger (discussed later) and has involved specific industries. This fact sheds light on the underlying drivers behind why mergers historically have occurred in waves. On one side, authors such as Shleifer and Vishny (2003) and Dong et al. (2006) consider stock market mis-valuation, especially since 1990, as a central driver for merger waves. The authors argue that bidders use overvalued shares to buy undervalued, or less overvalued, targets and thereby create value for their shareholders. This is further discussed in the *Valuation theory* below and in Section 2.4. On the other side (e.g., Harford, 2005; Gort, 1969), the argument is rather that restructuring from shocks in the economy or technology explains why mergers occur in waves. In other words, this argument states that value is created from efficiency-improving decisions which generate synergy gains. Whittington et al. (2020) conclude that M&A activity is broadly linked to factors such as changes in the global economy, stock market performance, availability of finance, new regulations and supply of target firms.

M&A can take different forms and two of the most common are *horizontal* and *vertical* deals (CFI, 2015). Horizontal M&A accounts for most of all M&A deals and occurs when companies in equivalent industries combine, with the purpose to create more value as a combined entity than on a standalone basis. Value creation from horizontal M&A is in general terms achieved through utilization of economies of scale, cost and revenue synergies through increased market power. M&A synergies are discussed in the *Efficiency theory* below. In addition, horizontal deals have other key strategic aspects, such as reduction of competition, which increase the market share of the acquiring company, as well as the combined entity's market power, resulting in bargaining power over suppliers and buyers. Vertical M&A instead involves companies in related lines of businesses, for example an acquisition of a supplier (backward vertical integration) or a distributor (forward vertical integration) in the same supply chain. This type of deal mainly requires a high degree of coordination instead of integration, which is a common factor to consider in horizontal deals. The main source of synergies in vertical M&A arise from cost reductions through control of the supply chain and other benefits from product diversification, as well as control over the product quality (Weber et al., 2013).

Although previous research tends to focus more on the consequences from M&A deals rather than the underlying motives, the field of research has brought forward several theories of merger motives (Trautwein, 1990). For example, merger theory exhaustively addresses financial, managerial and strategic motives for M&A (e.g. Whittington et al., 2020). In order to structure the following section, we turn to Trautwein (1990) who presents five organized key categories of common merger motives, summarized below.

Table 1

Summary of merger motive theories

<table>
<tr><td rowspan="4">Merger as a rational choice</td><td rowspan="3">Merger benefits bidder's shareholders</td><td>Net gains through synergies</td><td>Efficiency theory</td></tr>
<tr><td>Wealth transfers from customers</td><td>Monopoly theory</td></tr>
<tr><td>Net gains through private information</td><td>Valuation theory</td></tr>
<tr><td colspan="2">Merger benefits managers</td><td>Empire building theory</td></tr>
<tr><td colspan="3">Merger as process outcome</td><td>Process theory</td></tr>
</table>

Source: Authors' design based on Trautwein (1990)

Efficiency theory assumes that the main rationale behind mergers is achievement of synergies in the form of financial, operational and/or managerial synergies. Weber et al. (2013) go further, stating that synergies are actually the main incentive for M&A overall. *Financial synergies* lower the firm's cost of capital through: (1) increased size which may give access to capital, (2) internal capital market which may allocate capital more efficiently, or (3) lowering the systematic risk of the company portfolio through diversification. *Operational synergies* arise from the combination of businesses and include knowledge transfer, cost savings and possibility to offer unique products/services (Trautwein, 1990). For instance, shared resources in terms of sales force, distribution channels and support functions are common potential sources of cost-reduction synergies (Weber et al., 2013). Although operational synergies seem reasonable and are often used to motivate mergers, previous studies show mixed evidence. Ghosh (2001) finds weak evidence to support operational improvements from mergers, whereas Healy et al. (1992) show significant post-merger improvements in asset productivity that yields increased operating cash flow returns. *Managerial synergies* are realized when the target's performance benefit from bidder management's superior planning and monitoring abilities (Trautwein, 1990). Damodaran (2005) elaborates around the fact that synergies in general are a common motive in M&A, by raising the awareness that synergies often are used to justify huge premiums but are seldomly analyzed objectively. Whittington et al. (2020) add to this based on the intense M&A activity in economic peaks, which should raise questions whether large premium acquisitions are justified as target companies are likely to be highly priced in those periods. With regards to financial synergies, Trautwein (1990) highlights the theoretical criticism that financial synergies cannot be achieved in an efficient capital market. Trautwein further cites Kitching (1967) and Porter (1987), who identify managerial and operational synergies as evasive concepts for being seldomly realized.

Monopoly theory identifies market power as a strong rationale behind mergers, mainly realized in horizontal transactions, including reduction of competition and enhanced bargaining power (Trautwein, 1990). In fact, the first merger wave (1897-1904) has been called "the merger for monopoly", since the high concentration of horizontal deals consolidated markets and formed large corporations (Lipton, 2006). Monopoly power can be valuable, however while industry companies benefit from reduced competition, the acquiring company alone pays the costs (Berk and DeMarzo, 2013). In summary, monopoly theory implies wealth transfer from the customers (Trautwein, 1990), which antitrust laws function to mitigate (Berk and DeMarzo, 2013).

Valuation theory argues that information asymmetry about a target's value is a strong motive behind mergers when bidder managers possess more information than the stock market. Such unique information often includes potential advantages from a combined entity, value-creating improvements and/or detecting an undervalued target waiting to be sold. Consequently, this theory assumes a violation of efficient capital markets, just like the financial synergy argument (Trautwein, 1990). Shleifer and Vishny (2003) elaborate around this and highlight market valuations of merging firms as a motive behind mergers. In their model of stock-market-driven acquisitions, the authors identify mergers as a form of arbitrage, based on the assumption that rational managers exploit mis-valuations in the market. Whittington et al. (2020) acknowledge this view as a financial motive and state that companies with booming share prices strongly prefer to acquire targets with equity rather that with upfront cash. Bid structure and motives regarding financing alternatives are further discussed in Section 2.4. On the contrary, Wensley (1982) argues that valuation theory is not necessarily incompatible with efficient capital markets. He means that private information possessed by the bidder is revealed in the bid, which would imply the target's stock price to jump on announcement, putting the bidder in a winner's curse situation. In that sense, efficient markets prevent the possibility to capitalize on revealed private information, although undervalued firms still exist. On the other hand, Trautwein (1990) refers to Shackle (1969, 1972) who states that market participants are unable to incorporate bidder's private information nor evaluate what information the bid is based upon in the market price, due to the nature of private information and its ambiguity. Wensley (1982) adds by stating that private information is not one-dimensional since pieces of information varies between bidders. All in all, there is widespread evidence that valuation theory is a justification for mergers (Trautwein, 1990).

Empire building theory refers to managers' self-interest in maximizing their own utility instead of the shareholders' value in mergers (Trautwein, 1990). On the contrary, Kim and Canina (2013) find support that managers involved in M&A are motivated by value creation. According to Berk and DeMarzo (2013), managers prefer to run large firms and therefore take on investments to increase the size, although the investment might have negative NPV. Potential motives behind this are often prestige, higher salaries in large corporations and publicity, causing such managers to expand unprofitable divisions or overpay in acquisitions. Baker et al. (2012) examine the relationship between past operating performance and market reactions to M&A announcements. They find evidence that the empire building motive explains why markets react negatively on M&A deals by firms with past superior performance. In general terms, Berk and DeMarzo (2013) show that the median change in bidder's share price on announcement is close to zero, whereas targets experience gains explained by takeover premiums. All in all, the empire building theory has gotten attraction in business press although collected evidence is quite limited (Trautwein, 1990). However, authors such as Ravenscraft and Scherer (1987) find support from their case studies that empire building aspects play some role in M&A decisions.

Process theory is the fifth theory discussed by Trautwein (1990) and describes that strategic decisions not necessarily are based on rational choices. Instead, the theory suggests that decisions are affected by the process governed by one or multiple influences presented below. (1) Simplifications and incomplete evaluations as a result of individuals' lack of information processing abilities, (2) Organizational routines which implies that old solutions are applied to new problems, causing limited problem-solving rationality, and (3) Political power where tactical considerations and mutual adjustments dominate the process, as a consequence from political games within the organization. Regarding this theory, Weber et al. (2013) discuss manager hubris, which essentially implies self-confidence causing problems such as over-payment. In relation, Whittington et al. (2020) mention over-optimism which is most present in high peaks and causes managers to make irrational bids, which on a larger scale likely affects the global M&A activity.

Most mergers fail to create value for bidder shareholders. In fact, recent studies show that 83 percent of all deals in recent years fail to achieve set goals (Weber et al., 2013). Accordingly, substantial amount of research has been conducted to evaluate and map critical success factors. The first general conclusion is that target shareholders usually benefit from M&A, whilst the bidder often has neutral or negative effects, explained by a takeover premium paid to target shareholders. Therefore, it is crucial for bidders to determine a correct price to make a deal profitable, which assumes a solid valuation (Gaughan, 2005). In relation to price and valuation, timing and especially estimation of net synergies directly affect the risk of overpaying, as previously mentioned in this section. From an organizational standpoint, evidence shows that several aspects of the integration phase have considerable impact on the level of success (Weber et al., 2013). First, cultural differences are critical to handle, especially in horizontal deals involving businesses where people are important resources (Whittington, et al., 2020). Second, planning the integration process is crucial to take advantage of the full value from the transaction. For instance, to retain valuable employees such as management representatives (Davis, 2012). Finally, also related to planning, it is crucial to have a clear picture of the combined entity, which could imply divestment of assets in the target company (Clark and Mills, 2013).

2.3 Real estate

Portfolio managers have seriously started to consider real estate as an investment class in the last 20 years. The trend has been driven by real estate becoming widely available through securitized products, listed real estate companies and REITs[1]. Additionally, restrictions on pension funds have been relaxed to include real estate as an acceptable investment. One of the reasons for increased interest in real estate lies in the benefit of including real estate investments in traditional portfolios. Real estate as an asset class shows low correlation with stocks and a negative correlation with bonds, creating opportunities to improve the risk adjusted portfolio return by including real estate (Brueggeman and Fisher, 2016). The authors further look at differences between property types and countries, finding that different property types and metropolitan areas behave differently over time, where diversifying across property types and locations reduce the overall portfolio risk.

Demirci et al. (2020) investigate the impact of real estate portfolio diversification on the cost of debt, finding that real estate lenders reward well-diversified portfolios with lower lending rates. Morri and Cristanziani (2009) analyze the capital structure choice in public European real estate companies in the EPRA/NAREIT Europe Index, finding evidence that company asset size directly influences the amount of debt issued, confirming the hypothesis that debt is cheaper for bigger firms and issuance is affected by economies of scale.

Womack (2012) studies a sample of real estate mergers spanning three decades (1980-2008), finding evidence that real estate mergers occur because firms with superior management acquire targets with unexploited opportunities to cut costs and increase earnings. Furthermore, the results indicate that real estate mergers generally create wealth since shareholders at worst break even. Myers and Majluf (1984) conclude that the form of payment in M&A transactions generally contains information about the bidder, specifically when shares are used as payment, signaling that the bidding firm is overvalued. Thus, targets prefer cash transactions. In contrast, Campbell et al. (2001) show that the signal is not as strong for real estate acquisitions. Womack (2012)

[1] REIT = Real Estate Investment Trust. Similar to a mutual fund that pools capital from numerous investors for investment in income-generating real estate, with favorable tax treatment.

indicates that a mix of stock and cash is the most preferred method of payment in real estate M&A transactions, with payment of mostly stock used in approximately in 52 percent of transactions and mixes with a higher cash share in 45 percent of transactions. Lastly, other payment forms, such as debt assumptions, are rarely used and appear in only 3 percent of the sample transactions.

2.4 Financing in mergers and acquisitions

In general, companies can raise money through debt, equity and hybrid securities with a various range of characteristics. The ultimate goal is to find the optimal mix which maximizes the firm value, also referred to as the optimal capital structure. Equity often consists of common stock and warrants, whereas debt normally involves bank loans and bonds. As hybrid securities, convertible debt and preferred stock are the most common (Damodaran, 2005).

The trade-off between pros and cons with each instrument is exhaustively discussed in the literature, where the evaluation of capital structure is considered as a key consideration in financing M&A deals. Baker and Martin (2011) emphasize this based on the complexity and importance of M&A deals, whose financing decision has substantial impact on a firm's capital structure. Further, Myers and Majluf (1984) find that firms may refuse to issue stock, and therefore abstain valuable investment opportunities, based on a valuation perspective. The authors argue that issuing shares at a perceived bargain price may outweigh the positive NPV from the investment. Thus, avoidance (or delay) of issuing shares to fund an investment opportunity can be a positive signal, based on superior information of the stock value possessed by managers. Dong et al. (2006) find evidence that bidders are more highly valued relative to the targets, especially in equity offers, resulting in those bidders to prefer paying with stock. In summary, Dong et al. (2006) find that mis-valuation not only affects transactions, but also financing and investment decisions overall. Shleifer and Vishny (2003) specifically study valuation aspects in transactions. They find that market mispricing affects corporate policies including equity and debt issuance, dividends, share repurchases and investments, which in terms of M&A implies interesting findings. The authors share the view that stock acquisitions are made by overvalued acquirers and that this type of transaction is more likely to occur under three circumstances. First, when market valuations are high with a supply of overvalued bidders and relatively less overvalued targets. Secondly, synergies must be perceived by the market, which makes M&A attractive in the short-run and enable bidders to pay premium and still improve the long-run claim on capital. Thirdly, when target managers either have a short horizon or get paid off to accept the deal. Shleifer and Vishny (2003) conclude that firms have strong incentives to become overvalued to enable acquisitions with stock, but also to survive and grow in general terms where undervalued firms easily become takeover targets. In summary, M&A financing and bid structure are ultimately connected to dilution and leverage (Damodaran, 2005).

Capital structure decisions are also directly linked to credit rating, which essentially reflects the financial risk and credit quality of a company (Kisgen, 2006). As previously mentioned, M&A financing decisions in particular, have a substantial effect on the bidder's capital structure. Kisgen (2006) emphasizes that costs and benefits associated with different levels of credit rating, affect managers' decisions on capital structure. Further, the author finds evidence that firms on the edge to an up- or downgrade in credit rating tend to issue less debt relative to equity. Baker and Martin (2011) highlight the importance to achieve a so-called *investment grade rating* (e.g. S&P scale AAA–BBB-) since investment grade firms can benefit from lower financing costs. Another strong incentive to obtain investment grade is that investors such as financial institutions, mutual funds and insurance companies are required to invest in investment grade rated bonds. This implies that investment grade firms get access to a larger market and a broader investor base (Kisgen, 2006).

2.5 Government theory and privatization

Privatization of public activities involves a transaction where public assets are divested to private parties (Kohn, 2004). In general terms, most public services are tax financed in the Nordics, such as schools and health care. Related to privatization of those services, there is an ongoing debate whether the government should provide services in-house or outsource to private suppliers. On one side, the argument is that private suppliers can deliver such services at lower cost, whereas the other side disagree by stating that private suppliers are incentivized to cut costs and as a consequence deliver services of lower quality (Hart et al., 1997). As an example, the welfare system in Sweden opened up for private actors during the 1990s, mainly within social services, health care and the school system (Blomqvist, 2004). Guo and Willner (2017) elaborate that the motive behind the trend in Sweden is greater efficiency and quality of services. Furthermore, they also find a difference between political sides where the right-wing is more willing to privatize, and that the level of already achieved privatization, as well as political orientation of the majority in a municipality, explain politicians strive for (further) privatization.

In terms of social infrastructure properties, municipalities have traditionally owned the real estate used to supply public services. However, the privatization trend has raised the awareness of the possibility to sell properties to private companies and lease back the premises from the private party (Lind and Lundström, 2010). Additionally, Lind and Lundström (2010) find that the public sector can benefit from a sale-and-leaseback arrangement with a private counterparty, since it should decrease costs related to property management, release capital to finance other investment needs and also to achieve a more efficient use of space, which ultimately decrease the total rental cost. In relation, Hart et al. (1997) point towards the issue that governmental services cannot be exhaustively specified, causing an incomplete contract towards potential suppliers. The authors conclude that the contractual risk argues in favor of public in-house provision but also that privatization can be favorable if quality reducing activities can be prohibited.

3. Case study methodology

This section presents the research design of our qualitative single-case study, followed by the chosen method for data collection as well as an assessment of the research quality.

3.1 Research design

We have chosen to implement a single-case study to investigate the growth journey of SBB and the acquisition of Hemfosa. Given the context of an intense growth journey, enabled by key strategic components and critical events such as the Hemfosa acquisition, we find the single-case study design crucial to enable a comprehensive narrative. This view is acknowledged by authors such as Merriam (1994) and Eisenhardt (1989), who argue that a case study is preferable when the intention is to deeply investigate complex and dynamic events. Maxwell (2013) agrees and highlights that qualitative studies focus more on analyzing the process rather than the outcome, which implies understanding the participants' perspective in the given context. In addition, Gomm et al. (2000) find the case study method more frequently used in research since it appears to be more useful than was traditionally believed, especially in fields such as education. This adds further justification in our chosen research design, with regards to the purpose of this study to be used as material to build a case for teaching purposes. In summary, qualitative research focuses on specific people or situations, also named as the inductive approach (Maxwell, 2013).

Merriam (1994) states that the choice of research method also should depend on the amount of existing literature and previous research. The author suggests that case studies could develop new theory by testing, extending and clarifying already exhaustively covered subjects. Since previous research and existing theories covered in this paper are substantially explored, we find additional justification behind the choice of conducting a qualitative case study, in which we contribute to existing research by investigating a case in the specific real estate context. This implies that the research design is strongly connected to the research questions and the deep purpose of this study, as recommended by Brinkmann and Kvale (2015).

With support from existing theories in methodology, the chosen single-case study method generates two main advantages: (1) deep understanding of the narrative around the growth journey of SBB as well as the acquisition of Hemfosa, (2) enabling insight in a unique real estate segment and how this context affects strategy in terms of growth, financing, and acquisitions.

3.2 Data collection

The main source of primary data consists of interviews, summarized and presented below in Table 2. To collect a complete set of primary data that is multidimensional and reliable, we chose to conduct interviews with both dependent and independent interviewees. Where interviewees with operational influence in SBB or Hemfosa are categorized as dependent. As a result, collected data represent perceptions from various narratives and stakeholders throughout the case, which weighted together should provide validity and depth to the analysis.

Table 2
Summary of interviews

Interviewee	**Company and role during case**	**Current company and role**	**Dependence**
Ilija Batljan	SBB (CEO & founder)	SBB (CEO & founder)	Dependent
Oscar Lekander	SBB (Business development manager)	SBB (Business development manager)	Dependent
Lennart Schuss	SBB (Chairman)	SBB (Chairman)	Dependent
Sven-Olof Johansson	SBB (Board member)	SBB (Board member)	Dependent
Lars Thagesson	SBB (Deputy CEO & COO) *	SBB (Deputy CEO & COO)	Dependent
Bengt Kjell	Hemfosa (Chairman)	Multiple involvements **	Dependent
Ulrika Lindmark	Newsec (Head of Valuation & Strategic Analysis)	Newsec (Head of Valuation & Strategic Analysis)	Independent
Tobias Kaj	ABG Sundal Collier (Analyst)	ABG Sundal Collier (Analyst)	Independent
Analyst	Anonymous	Anonymous	Independent
Samuel Lundqvist	Skellefteå municipality (CFO)	Skellefteå municipality (CFO)	Independent
Mats Gerdau	Nacka municipality (Chairman)	Nacka municipality (Chairman)	Independent

* *Previously founding partner and COO at Hemfosa Fastigheter AB. Thagesson joined SBB in February 2018*
** *Chairman of SSAB, board member of Industrivärlden, Pandox and Indutrade etc.*

Source: Authors

Since interviews are the main source of data in this study the interview process is crucial. To ensure quality of the process, we have used steps 1-4 in the framework by Brinkmann & Kvale (2015): (1) Thematizing, (2) Designing, (3) Interviewing, (4) Transcribing, described below.

Thematizing is the initial stage in which we formulated the purpose of the study. First, we decided to conduct an explorative study which entails open-ended interviews with limited structure compared to hypothesis-testing studies. According to Eisenhardt (1989), explorative studies are the most natural to implement in qualitative research. In the next step, we gathered background information and existing research (presented in sections 2 and 4) relevant for the scope of the study and to enable relevant and concentrated interviews.

Design is the second step of the framework where we answered the question *how* to collect the data. First, we took the whole process into consideration, including the timeframe and resources for the scope of the study. Second, the preparation proceeded by a thorough research on the companies and potential interviewees, which is important in order to obtain the intended knowledge and data from upcoming interviews. Finally, we arrived at eleven desired interviewees which fulfilled the two most crucial requirements, namely: a doable but still sufficient sample of primary data and representatives from all relevant angles in the study.

Interviews were conducted based on the sample of interviewees presented in Table 2. Barbour (2014) stresses the importance to find a balance between the researcher’s agenda, open-ended questions, detailed follow-up questions and the ability to leave space for participants to reflect and share insights. Therefore, we strived to lead the conversation through short and open questions, followed by detailed follow-up questions based on the interviewee's response. Prior to interviews, the content for each interview were sent to contact persons, enabling preparation and hence the interviewees ability to share high-quality answers. The interview questions varied depending on the interviewee. For company representatives as an example, the questions were divided into four sections: personal background, company background, the Hemfosa acquisition and the real estate market.

Transcribing of interviews was carried out immediately after each interview in a word-by-word format. The interviews were recorded on tape with an average duration of approximately one hour, which enabled us as interviewers to be more present. As an initial step of the data analysis, transcribing was important since new observations and information could be used in subsequent interviews.

3.3 Research quality

Although the single-case study has its benefits, the method also has several imperfections. Yin (2014) and Maxwell (2013), among others, raise concerns for single-case studies regarding the uniqueness of each case, which causes vulnerability in terms of inadequate generalization and insufficient analytical conclusions. Consequently, this section aims to elaborate around the view on research quality of this study, which also facilitates evaluation from the reader's perspective. Yin (2014) discusses criticism by introducing several tactics in the four principles commonly used to establish quality in case study research. The principles and the arrangements we have taken to ensure the research quality are presented below.

Construct validity is a significant challenge in case study research and refers to subjectivity in data collection, which violates the construct validity. To ensure that our study measures what we claim, the following has been done based on the proposed tactics put forward by Yin (2014). First, we use multiple sources of data in terms of primary and secondary data as well as both dependent and independent interviewees. Secondly, the final draft was sent to all participants for review, which should give legitimacy to the content.

Internal validity mainly addresses the concern in explanatory case studies regarding incorrect conclusions of a causal relationship. We mitigate this risk by taking the measures already mentioned, but also through pattern matching which implies that causal relationships are matched from multiple sources.

External validity raises the problem around generalizability of case studies, with authors such as Silverman (2017) who argue that single-case studies cannot be generalized. Consequently, single-case studies have limited external validity. With that said, the conclusions from this study should only be considered valid in the specific context. However, we would argue that aspects of the growth journey of SBB, as well as the motives behind the Hemfosa acquisition, could be useful for comparable cases and future research, especially within Nordic real estate.

Reliability is the final principle and addresses the replicability of the study. Thus, in the previous sections of this chapter, methods for research design and data collection are presented to provide transparency. One could question whether our explorative study is possible to replicate and therefore, interview questions, recordings and transcripts have been collected to anyone interested in replicating the study, as recommended by Yin (2014).

Apart from the general critique against single-case studies, we also want to assess specific factors affecting the research quality of this study. On the one hand, we see three main advantages. First, with regards to the timeframe, we identify an advantage in the quality of the data since the Hemfosa transaction took place less than a year ago from the date of this study. Secondly, interviews have intentionally been conducted in Swedish to enable participants to express themselves in their native language, which should contribute to more qualitative answers. Thirdly, we would argue that interviewees' experience, reputation and outstanding track-record provide high-quality primary data. On the other hand, there are aspects with potential negative impact on the research quality. First, five out of twelve interviews were conducted digitally both due to Covid-19 and distance, which may impact the quality of those interviews. Second, the primary data could have been more equally weighted since only one interviewee represent Hemfosa at the time of the acquisition. However, we feel confident that Bengt Kjell, as Chairman of the board and lead negotiator, can represent the view of Hemfosa. Third, one must keep in mind that SBB is a public company and that M&A deals involve confidentiality, which may have put constraints on the ability to share complete answers to all questions, especially related to the acquisition.

4. Market background

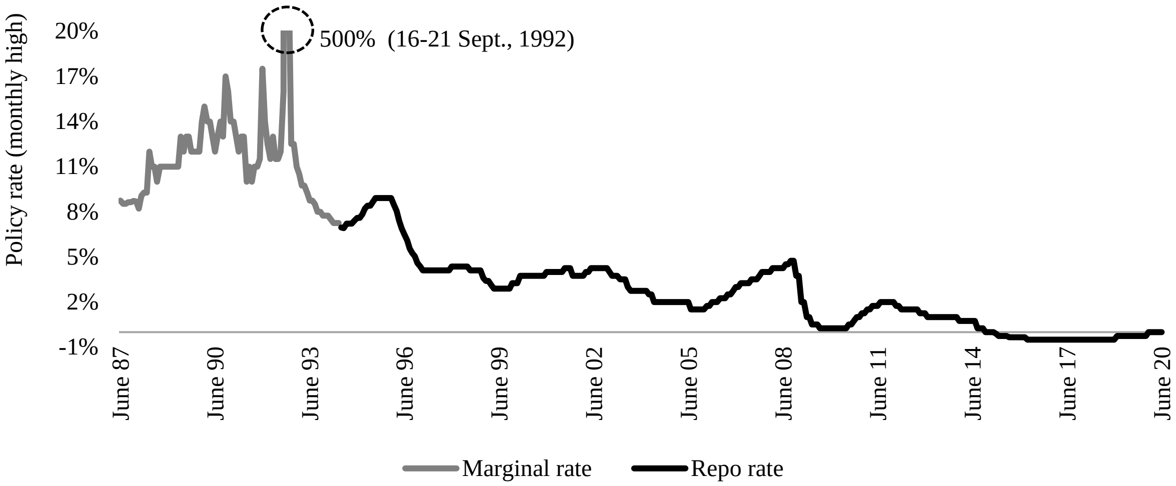
This section presents relevant market background as a foundation for the case study, covering the real estate market and welfare system, demographic development and key segments within the Nordic real estate market, including the role of Swedish municipalities.

4.1 The real estate market

A prerequisite for a well-functioning and growing real estate market is access to financing, since almost everyone relies on external financing to operate a real estate business (Lindmark, 23.10.2020). Consequently, the real estate industry has experienced an astonishing development as interest rates have dropped consistently since 1994 (Johansson, 19.10.2020).

Figure 1

Riksbank policy rate (June 1987 – June 2020)



Source: Swedish Riksbank

The current era was preceded by a crisis during the early 1990s, when the Swedish Riksbank attempted to protect the value of the Swedish Krona, that was pegged with a fixed exchange rate to the ECU[2]. Consequently, the interest rate situation changed in a dramatic way as the Riksbank's policy rate peaked at 500 percent between September 16th and September 21st, 1992, causing severe problems for the real estate industry (Johansson 19.10.2020). This was predated by a tax reform in 1991, which reduced the right of tax deductibility on interest payments from 50 percent to 30 percent (Finansdepartementet, 1997), that increased effective interest expenses, putting pressure on highly leveraged real estate companies. During this crisis, plenty of companies went bankrupt and the industry was radically restructured, were banks became owners of large real estate portfolios. Several prominent Swedish real estate companies today are products of restructuring during these years, Fabege, Klövern and Wihlborgs to name a few (Schuss, 16.10.2020). The 1990s crisis laid the foundation for a new monetary policy with focus on price stability and controlling inflation (Riksbank, 2020).

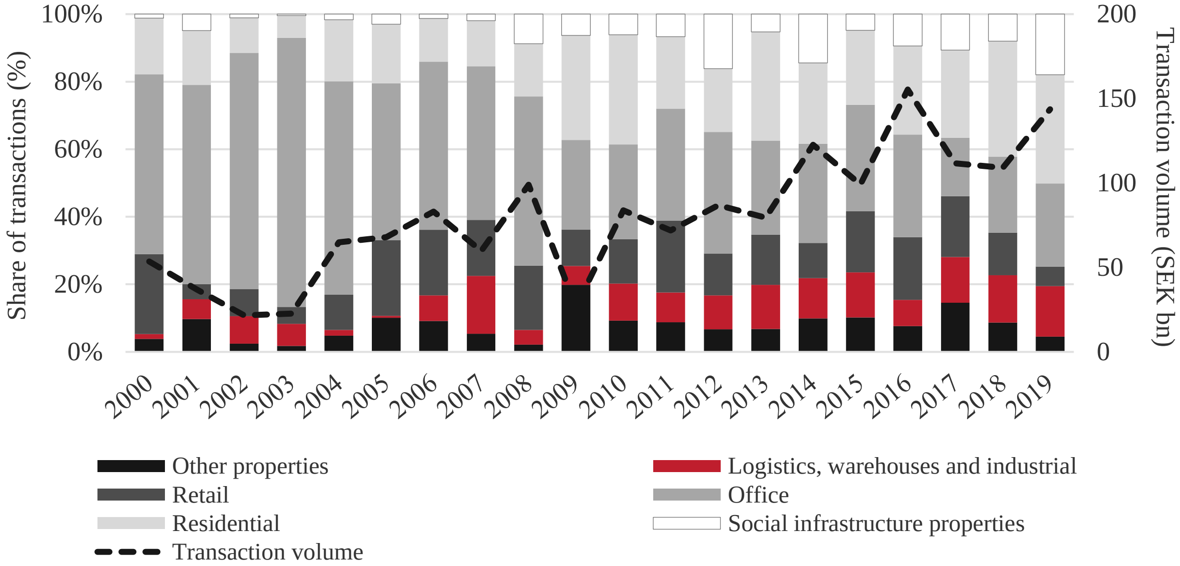
Since then, the bond market which real estate companies use a lot, has experienced a favorable development both in terms maturity and volume, especially for rated companies. Also, in subsequent crises the Central banks globally have used quantitative easing programs to provide liquidity, by using their balance sheets to purchase both government and corporate bonds. *"The conditions have been fantastic for real estate companies to finance themselves and this has enabled a large part of the growth during the past decades."* (Johansson 19.10.2020). Today, the Nordic market has developed into one of the world's most liquid real estate markets and is expected to continue to be so with a growing interest from international investors, complementing a large domestic investor base. The increased attractiveness can partly be explained by attaining a status as a safe haven destination for yield-seeking investors, as a result of the central banks' low

[2] A basket of European Economic Community country currencies

policy rates and a stable political environment (SBB, 2019e). Figure 2 shows the development of transaction volumes (SEK >100m) in Sweden between 2000-2019, and during this period, the social infrastructure real estate segment has taken form. Today, Sweden is the most mature and leading market within this segment, that has recently been established in Denmark, Finland and Norway, where the respective markets are in different phases of development (Lindmark, 23.10.2020). The main drivers behind forming the social infrastructure segment is the strong Nordic welfare system and demographic trends that put pressure on investments in the public sector, which has enabled private companies to enter the market (Fastighetsvärlden, 2017).

Figure 2

Swedish real estate transaction volumes (2000 – 2019)



Source: Newsec

4.2 The Nordic welfare system

The Nordic countries are unique on a global scale with societies based on a strong welfare model. The model is characterized by a prominent public sector, that provides citizens with welfare services and an extensive social safety net. Specifically, this includes health services, hospitals, elderly care, child benefits and parental leave, all of which are taxpayer funded and free for everyone at the point of delivery (Nordic Co-operation, 2020).

In all Nordic countries, legislation prevents local authorities from declaring bankruptcy, which implies that the state intervenes if a regional or local authority would experience financial distress. As a result, no Nordic municipality or county council has defaulted in the last century, although some have experienced financial distress (Moody's, 2018). Appendix 10.1 presents examples of state interventions in municipalities that have experienced financial distress.

4.3 Nordic demographic outlook

The global trend of urbanization and an aging population is also found in the Nordic region, with the largest increases in population expected in urban and suburban areas. The urbanization trend applies not only to the largest cities, but also regional cities and is similar in all the Nordic countries. In addition, the demographic development clearly shows an aging population. Looking at the OADR[3] measure, data shows an increase in the Nordic region from approximately 24 percent in 1990 to 30 percent in 2017. By 2040, the ratio is estimated to reach 40 percent. The increasing OADR shows no signs of slowing down, instead further increases after 2040 appear likely (Nordregio, 2019). Appendix 10.2 illustrates Nordic population forecasts until 2040.

The aging population puts pressure on the welfare states, where the organization and funding of health care and elderly support are major concerns. This has led to the public sector struggling to finance increased investment needs to cater for a growing and aging population, by tax income from a shrinking working age population (Bengtsson and Scott, 2011). None of the potential financing solutions including increased tax rates, additional borrowing or selling assets are very well perceived by the public. See Appendix 10.2 for more detailed information.

4.4 Social infrastructure properties

Definition

Social infrastructure properties can be defined as: Property that is used predominantly for tax-financed activities and is specifically adapted for community services. In addition, extra-care housing is included under the concept of social infrastructure properties (Fastighetsvärlden, 2014a). Further, these properties are divided into five sub-categories: judiciary, education and childcare, recreation, health care and adapted housing.

Table 3

Social infrastructure sub-sectors

Judiciary	Education & Childcare	Recreation	Health care	Adapted housing
Courts	Universities and Higher education	Bathing- and sports facilities	Hospitals	Extra-care housing
Police facilities	Other school	Churches	Health centers	Special care housing
Prisons/detention facilities	Childcare	Cultural buildings	Dentist facilities	LSS housing
Other judiciary facilities			Other health care facilities	Elderly care
				Dormitories

Source: Fastighetsvärlden, 2014a

However, this definition is not statutory, making it important to be aware of how different actors use the term *social infrastructure property*. Examples of what is not counted as social infrastructure according to the definition are municipal administrative buildings, and buildings with, for example, the Swedish Tax Agency as tenant.

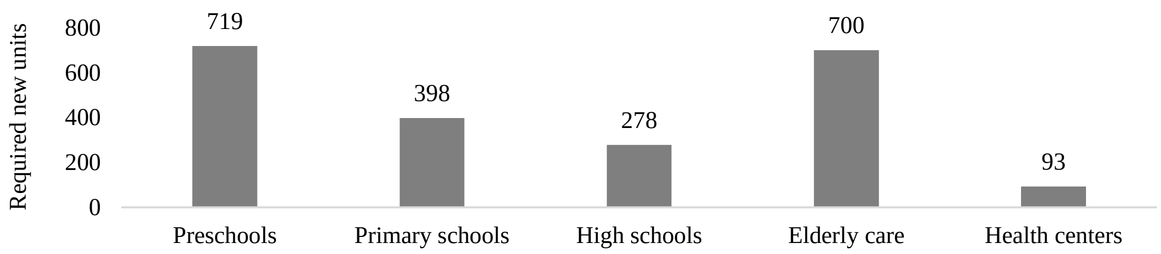
[3] Old-Age Dependency Ratio (“OADR”), measuring people at +65 years, as a proportion to the number of people aged 15 to 64.

Demand

The demographic aspects covered in Section 4.3 have a natural connection to the need for social infrastructure properties. Figure 3 shows the demand for new investments in Sweden until 2026. For instance, this shows an average investment need of almost 2.5 elderly care homes and 4.8 new schools in each Swedish municipality. The other Nordic countries also experience the same type of demographic change as in Sweden and therefore a similar need for investments to cater for the population. In summary, the increased demand for investments, in combination with financial constraints in the public sector, has created opportunities for private owners of real estate to finance investments in exchange for long-term lease contracts backed by the Nordic welfare states.

Figure 3

Investment need for new units 2019-2026



Source: SCB, Swedish Ministry of Finance

Contracts and regulation

Given the implicit state support and the ability for municipalities and county councils to levy taxes, the counterparty risk towards the public sector is significantly lower compared to leases with commercial counterparties (Moody's, 2018). The leases for social infrastructure properties are similar in all Nordic countries and do typically not differ from commercial leases in terms of structure. The base rent in the lease is generally adjusted by an indexation clause tied to the local consumer price index, creating an inflation protected income stream. It requires a minimum lease term of three years to be able to include an indexation clause in the contract. However, it is possible to negotiate a fixed annual supplement for shorter contracts (Fastighetsägarna, 2020). Due to tenant's creditworthiness and property purpose-specific specialization, long contracts of up to 20 years are common, in comparison to commercial property segments (e.g. office and retail) where contracts instead normally extend over three to five years (Finansinspektionen, 2019).

In general, public authorities need to go through a public procurement process for all major purchases or agreements that involve financial obligations. However, the lease of existing premises is generally exempt from this requirement. Signing a lease for a building under construction can also be excluded, but only if the building is not designed according to specific guidance from the public tenant, which is usually the case for education, healthcare and judicial properties. The degree of specialization depends on the type of tenant, and the tenants' tendency to extend their lease at the end of the lease term. Appendix 10.3 illustrates the relationship between the degree of specialization and the tendency to extend the lease for different types of properties.

The market

As an investment, social infrastructure properties have many strengths. First, it is relatively easy to assess the long-term demand for the current business, based on demographic forecasts, which is generally increasing. Secondly, as mentioned, lease contracts have long durations towards low-risk counterparties (public/public-financed private operators) and are likely to be extended at maturity. Finally, the location is not as crucial as for other property segments (Svefa, 2019).

There are two main risks when evaluating investments in the sector. First, there is a reputational risk, putting higher demands on the property owner to act responsibly when managing this type of assets. Secondly, there is a residual value risk if a tenant moves out, that might lead to costly conversions or a long vacancy period (Svefa, 2019). However, high specialization implies a lock-in effect and limits the supply of equivalent alternatives. Furthermore, existing properties with low book values and lower rents have a comparative advantage in terms of price. This implies another lock-in effect for tenants, especially if evaluating new construction (Kaj, 16.10.2020).

Given the aforementioned factors, interest in social infrastructure properties has grown rapidly, from a few market participants five years ago to over 50 more or less established companies active in the sector. Investors range from pension-backed institutional investors and listed real estate companies such as SBB, Balder and Heba to specialist funds managed by NREP, Capman and Northern Horizon. As a result, the segment has been established and is growing through new construction and specialization. So far, the public sector, that is still dominant in terms of ownership share, has accounted for a small share of transactions (Svefa, 2019).

The increased interest in the asset class has put pressure on the required rate of return, causing yields[4] to decrease over time. Appendix 10.4 shows yield development and rents levels for different types of social infrastructure properties in the Nordic market. *"If you chase a good return at low risk, then both social infrastructure properties and residentials are very good, social infrastructure in particular due to the yield gap"* (Lindmark, 23.10.2020).

4.5 Residential properties

Regulated rental apartments (Swe: Hyresrätt) are the most common type of apartment in Sweden, amounting to 58 percent of total apartments, approximately 1.5 million dwellings. Residents in those apartments rent directly from a real estate company. In Sweden, rental apartments are most common in 257 out of 290 municipalities (SCB, 2019). Rents in these apartments are strictly regulated, presented in the next paragraph. The remaining 42 percent of apartments are called *housing cooperative apartments (Swe: Bostadsrätt)*. People living in those apartments are

[4] Rate of return measure in real estate, calculated as: Net operating income / Asset value

members of a housing association, a legal entity that owns the building. The owner of a cooperative apartment does not own the apartment itself, but a share in the association, giving the owner the right to use a specified apartment until the share is sold (Bostadsrättslag, 1991). Unit-owned apartments, *condominiums* (*Swe: Äganderätt*), which are common in other countries, is a relatively new form of housing in Sweden that was approved by law in 2009 (Regeringskansliet, 2013). Therefore, the market for condominiums is almost non-existent with only about 1,300 apartments (SCB, 2019).

Rents and regulations

Sweden has two major systems for pricing in rental apartments: *value-in-use rents* and *presumptive rents*. Rental apartments built before 2006, are regulated according to the value-in-use system (Jordabalk, 1970). The pricing is based on comparable apartments with similar standards, location, equipment and fees. For example, renovations increase the value-in-use and therefore the rent must always be renegotiated after improvements. In order to protect the tenants, landlords need the tenants' consent to perform improvements in individual apartments and the consent of more than half of the affected tenants for common use improvements, such as laundry room and elevator. The subject of value improving renovation is a politically sensitive subject as older apartments with neglected maintenance can have rents increased by as much as 50 percent after renovation, leading to the previous residents no longer affording to stay (GP, 2019). This debate has intensified as international players have entered the market, starting to renovate whole building blocks. *"Private equity companies have been quite insensitive in how renovations have been conducted, emptying entire buildings for renovation and raising rents"* (Johansson, 19.10.2020). How rents are set for apartments built after 2006 using presumptive rent setting, is presented in Appendix 10.5.

Supply and demand

As urbanization progresses, cities are expected to experience continued population growth and thus maintain a high demand for housing. Currently, 74 percent of Swedish municipalities report housing deficits and only 3 percent report a surplus (Boverket, 2019). To put this in context, over 675,000 people were registered in line for apartments at the Stockholm housing agency in the end of 2019, in comparison to only ~15,000 apartments brokered for the full year 2019 (Bostadsförmedlingen, 2019). Thus, to bridge the supply and demand gap, it would require annual new construction of ~65,000 dwellings until 2027. However, construction forecasts so far indicate that the gap is more likely to widen in the coming years (Boverket, 2020). In combination with regulated rents, investments in Swedish residential apartments are thus considered safe, due to an extremely low tenant dependency (SBB, 2019a).

4.6 The role of municipalities

Traditionally, the public sector has been the sole owner (indirectly or directly) of social infrastructure and rent-regulated housing properties. However, Swedish municipalities have started to cooperate with private companies to get support in building the communities, especially in growing municipalities with fewer private actors in their respective market. *"The absolute purpose is to get large private investors to invest their capital in the region. The main purpose for us is not to raise capital and liquidity, nor lower rents because we know that rents are higher from private parties. Higher rent is the price you have to pay to attract large private companies."* (Lundqvist, 02.11.2020). In relation, the private side acknowledges this view since private real estate companies contribute to the societal development by building infrastructure (Johansson, 19.10.2020). *"We build 10-20 elderly care properties annually and a municipality builds one such property every 20 years. We should therefore be able to build more efficiently."* (Lekander, 19.10.2020). Additionally, Bergvall and Von Bahr (2020) find that municipalities in general are positive to sell building rights as a way to get private companies into the market, as this both generates municipal income and allows the public sector to control what is built. However, it is judicially hard to get commitments from private investors to continue investing, but private actors must live up to expectations to be considered in future projects (Lundqvist, 02.11.2020).

Depending on the level of municipalities' property management organizations, another motive behind privatization is competition from professional parties and benchmarking of internal capabilities, as was recently the case for Nacka municipality (Gerdau, 27.10.2020). On the contrary, this was not a motive for Skellefteå municipality with established property management (Lundqvist, 02.11.2020). From a private perspective, the operational motive is reasonable since real estate is not a municipality's core business, and the motive gets even more significant for municipalities without professional organizations (Batljan, 14.10.2020).

Raising capital and avoiding excessive borrowing is also stated as a reason behind privatization in the market, since capital generated from real estate divestments can be used for other municipal investments. In comparison with real estate companies, municipalities have several business areas that need maintenance and investment, requiring a holistic perspective on the best use of the tax-payers money (Gerdau, 27.10.2020). Municipalities struggling with their finances often end up selling assets to private companies (Johansson, 19.10.2020). On the contrary, this motive rather becomes a spill-over effect in municipalities with strong finances (Lundqvist, 02.11.2020).

The decision-making process for new investments and divestments follows a political process, where the municipal board votes on a proposal and can sign into agreements subject to a majority decision. A key consideration in the process from a municipal point of view is finding professional actors with a long-term perspective that can live up to the expectations, since municipalities in most cases remain as tenants in the premises over long horizons (Gerdau, 27.10.2020; Lundqvist, 02.11.2020). *"In the transaction where SBB ended up as buyers, we offered a fixed purchase price of SEK 1,050mn. Instead, the potential buyers competed solely on the lease agreement terms: rent and duration."* (Lundqvist, 02.11.2020). In sales processes involving real estate, municipalities hire professional transaction advisors through public procurement processes, in order to maximize the transaction value from a competitive bidding process (Gerdau, 27.10.2020; Lundqvist, 02.11.2020).

The major dilemma municipalities face when cooperating with private companies is moral hazard, in situations with conflicting interests (Bergvall and Von Bahr, 2020). This stresses the importance of finding the right counterparty and monitoring to make sure contract obligations are followed. Opponents of privatization usually argue for ideological reasons, opposing to give away control of public assets to third parties. *"In the earlier transactions the right-wing parties have been supporting whereas the left-wing has opposed the divestments"* (Gerdau, 27.10.2020).

5. Company and case background

This chapter introduces the relevant companies and individuals, including growth journeys, business models and conditions, to provide a complete foundation leading into the case.

5.1 Introduction

Ilija Batljan

On December 9th, 2015, a shocking announcement struck the Swedish real estate market when Rikshem, a leading real estate company, published the news that Ilija Batljan, deputy CEO, had been fired with immediate effect (Fastighetsvärlden, 2015). During his five years at Rikshem, Batljan had played a key role in establishing the company, including the responsibility of growing the property portfolio to SEK ~35bn from scratch and achieving a A- credit rating from S&P. Thus, becoming the first Swedish private real estate company to attain an investment grade credit rating (Batljan, 14.10.2020).

Prior to his employment at Rikshem, in the early stages of his career, Batljan worked with programming and developed a keen interest in theoretical mathematics and economics. After immigrating from Bosnia Herzegovina to Sweden in the early 1990s, Batljan studied a bachelor's degree and eventually moved into politics, where he served as Mayor, deputy County Commissioner, civil servant and advisor to the Swedish government. During his time as the Head of Analysis at the Ministry of Social Affairs, Batljan built models on demographics and started to develop an interest in the aging population. At this point, Batljan chose to pursue Ph.D. studies, resulting in a Ph.D. degree in 2007, where he built a model to forecast future demand for care and nursing, which later turned out to be fundamental in the founding of SBB (Batljan, 14.10.2020).

In parallel with his political career, Batljan invested in several IT companies, which enabled him to accumulate capital gains as well as the experience to develop companies, for instance from being Chairman of the listed company Cryptzone. Additionally, also parallel to politics, Batljan met with Lars Thagesson (later one of the founders of Hemfosa), who had identified a great potential to invest in Swedish elderly care properties. At this point, Batljan realized he had to start a real estate company and therefore decided to end his political involvement at the end of the ongoing term. As a first step towards real estate, Batljan was involved as a consultant in the founding process of Hemfosa in 2009. During his last year in politics (2010-2011), Batljan reached out to AP4 in a second attempt to start his real estate company, but instead ended up as deputy CEO and Head of Social Infrastructure in establishing Rikshem (Rikshem, 2011; Batljan, 14.10.2020). After being dismissed from Rikshem in 2015, Batljan saw a third chance to start his real estate company. On the day he left Rikshem, several individuals from the real estate industry reached out offering job opportunities, investment capital, lawyers and office space. From this point, the founding of SBB had begun (Batljan, 14.10.2020).

SBB

The initial step in founding SBB was to build a platform with the right people. Therefore, Batljan contacted his friend Lennart Schuss, invited him for lunch at his favorite restaurant and offered him to become Chairman of the board (Batljan, 14.10.2020; Schuss, 16.10.2020). Schuss has an extensive background, especially in M&A from being involved in transactions totaling SEK 500bn and had previously founded Catella Corporate Finance and the real estate company Gimmel. *"I have probably been involved in founding most of the listed real estate companies you see today: Fabage, Klövern, Wihlborgs, among others."* (Schuss, 16.10.2020). Six months after joining SBB, Schuss and his founding partners at Gimmel, Sven-Olof Johansson and Erik Paulsson, agreed on SBB to make a non-cash acquisition of Gimmel's real estate portfolio in exchange for SBB shares (Schuss, 16.10.2020). Paulsson, founder of the construction company PEAB and Johansson, CEO of Fastpartner, two role models for Batljan, each held 8 percent in SBB after the deal, including private add-on investments of SEK 100mn in newly issued B-shares (Fastighetsvärlden, 2016a). *"One could say that the start-up capital, together with Ilija's invested capital, came from this deal."* (Johansson, 19.10.2020). Apart from being one of the major shareholders, Johansson with his valuable background, also became a member of the SBB board. Johansson had namely started his career in real estate already in the 1980s, served (and still serves) as the CEO of Fastpartner since 1996 and had witnessed the crises both in the 1990s, the dotcom crisis, and the global financial crisis in 2008 (Johansson, 19.10.2020).

In order to establish the platform, Batljan also reached out to recruit former colleagues at Rikshem, including the Head of Investments, Oscar Lekander. *"We had experience from working closely together at Rikshem, which really is one of the strengths in SBB and the key to keep the* *high-paced growth. We knew our roles from the beginning."* (Lekander, 19.10.2020). Lekander had previously studied his bachelor and master's degree in real estate and finance before joining Rikshem in 2013. After receiving the call from Batljan in the spring of 2016, Lekander decided to join SBB as Business Development Manager (Lekander, 19.10.2020).

With the platform of experienced individuals and the start-up capital put in place, SBB now started an intense growth journey with focus on residential and social infrastructure properties in Sweden, and eventually also in Norway, Finland and Denmark.

Lars Thagesson

Born and raised in an entrepreneurial family, Thagesson founded his first real estate company already in 1978, four years after finishing high school. With his impulsion to build and create, Thagesson was eventually part of pioneering the segment for social infrastructure (Thagesson, 28.10.2020).

During the 1990s, when the Swedish financial market collapsed and real estate companies found themselves in severe financial distress, banks were forced to realize real estate pledged as security for loans. Lars Thagesson was hired by Gota Bank in 1993 to redeem properties from defaulted borrowers and manage a rapidly growing property portfolio in the bank's asset company called Kungsleden, with the plan to liquidate the seized assets (Thagesson, 28.10.2020).

With most of the portfolio disposed by 1998, the team at Kungsleden wanted to preserve the organization they had built up. Led by CEO Jens Engwall and COO Lars Thagesson they received institutional backing to take over the company, changing focus from liquidating assets to growth. Kungsleden was listed in 1999, and continued to grow through opportunistic acquisitions across Sweden, pioneering the social infrastructure segment. *"Gradually, we concluded that it is safe to have the state, municipalities and county councils as tenants with long agreements, since one gets rental income regardless of the state of the world. It took a while for others to realize this."* (Thagesson, 28.10.2020). The social infrastructure portfolio was later separated into a company called Hemsö and sold to Swedish pension fund AP3, leaving Kungsleden as a pure commercial real estate company. In the wake of the global financial crisis, Thagesson, Engwall and Bengt Kjell, Chairman of Kungsleden, left the company to start a new venture, Hemfosa (Thagesson, 28.10.2020).

Hemfosa

Hemfosa was founded in 2009 to exploit a gap in the market left by Kungsleden, who had turned away from high yielding assets to focus on building clustered portfolios (Thagesson, 28.10.2020). To quickly seize opportunities in a moving real estate market, the founders built a team by recruiting two former colleagues at Kungsleden, with competence in business development and real estate law, as well as a CFO from AP3 (Thagesson, 28.10.2020; Hemfosa, 2014). The implemented business model was completely opportunistic, targeting properties with high cash-yield regardless of location or sector, in order to maximize the yield-spread between operating cash flow and interest expenses (Kjell, 10.11.2020).

With the help of Lennart Schuss and Catella, the team raised SEK 2bn in equity from institutional investors to replicate what Kungsleden had done ten years prior (Thagesson, 28.10.2020). *"After Lehman Brothers, when companies started to file for bankruptcy, we sat at an auction four days a week for three weeks and called in basically everything on behalf of Hemfosa. The company was initially built on others insolvency."* (Thagesson, 28.10.2020).

5.2 Company backgrounds

5.2.1 SBB

Business model

Already from the beginning, based on his experience and modelling, Batljan had a clear view on the business model of SBB. With the platform of key individuals as a foundation (Batljan, 14.10.2020), the business model is set to create a stable cash flow machine (SBB, 2019a) built on the following cornerstones: (1) core holdings in residential and social infrastructure properties, (2) focus on credit rating, (3) wide financing base, (4) non-cash acquisitions, and (5) scale.

Figure 4

Cornerstones in the business model of SBB

Source: Authors based on company reports and interviews

(1) SBB's overall strategy is to be a long-term owner who manages and develops rent-regulated residential properties in Sweden and social infrastructure properties in the Nordics. SBB aims to acquire relatively cheap properties in terms of rent per sq.m. (see Appendix 10.6), which are associated with lower residual value risk due to the absence of cheaper substitutes. The strategy also enables property development to acquire building rights[5] (Lekander, 19.10.2020). *Social infrastructure properties* constitute the bulk of SBB's portfolio to safeguard stability (SBB, 2019a), since those generate government-secured cash flows over long lease durations, presented in Appendix 10.6 (Johansson, 19.10.2020). The holdings mainly include elderly homes, properties for disabled and schools, where the tenants are, directly or indirectly, municipalities and state. Social infrastructure properties are acquired from other real estate companies and the public sector (municipalities). Consequently, a fundamental aspect is the relationship with municipalities,

[5] The right a property owner has to build on a plot. For example, what the land/building may be used for, how many sq.m. may be built, maximum number of floors, building height, and minimum distance to plot boundary and between buildings.

which SBB has built over time by demonstrating a long-term view and a trustworthy deal team (Batljan, 14.10.2020). In relation, there are analysts that agree and further highlight Batljan's political background as a great asset in negotiation of acquisitions and contracts with public parties (Erik Penser Bank, 2019b). *"The benefit from my political background is rather that I understand how the system works. If I initiate a deal today, we may end up closing it in three years. Apart from that, it is all about how you conduct business because municipalities talk to each other"* (Batljan, 14.10.2020). The SBB portfolio also comprises a significant share of *Residential properties* in Sweden. At the end of 2019, SBB owned residential properties in 30 cities across Sweden, totaling 13,300 rent-regulated apartments. In relation to this segment, SBB has a strategy to renovate around 600 apartments annually (SBB, 2019a). However, due to a sensitive political debate on rent increases, driven by the entrance of short-term investment companies that renovate apartments to gain from substantial rent increases, SBB has taken precaution to be responsible in renovation and raising rents (Johansson, 19.10.2020). Altogether, based on the footprint in the two mentioned segments, SBB became the first private member of "Svenska Allmännyttan[6]" in September 2019, which enhances the reputation of being a long-term partner to the public sector (SBB, 2019a). The remaining part of the portfolio is *Other*, which involves development of building rights from properties with identified potential, that generate cash flows until a detailed development plan[7] is set. Most of the acquisitions in this segment are made off market after a dialogue with municipalities, ensuring that the properties are prioritized in future urban development (SBB, 2019a). *"Property development is an important part of our business model. We work closely in the organization to identify potential to create building rights or to refine our properties."* (Lekander, 19.10.2020).

(2) Based on Batljan's keen interest in credit ratings, SBB has from day one been focused on attaining a credit rating and eventually an investment grade rating (Batljan, 14.10.2020). Therefore, the company's capital structure is carefully considered, described in the next paragraph. This awareness has been crucial for SBB and the current investment grade rating (BBB-) has enabled cost-efficient access to capital from a larger market, which paves the way for growth in the company (Johansson, 19.10.2020). Going forward, the goal is to improve the rating to BBB+, which SBB considers to be of highest importance to achieve stability. For this reason, the company works actively on improving the equity ratio (Schuss, 16.10.2020). The credit rating is also connected to size and diversification of the property portfolio (Johansson, 19.10.2020) and is directly decisive for the ability to grow from acquisitions. *"We cannot grow faster than our balance sheet can support. The prioritized goal is to improve our rating"* (Lekander, 19.10.2020).

[6] Svenska Allmännyttan consists of municipal residential real estate companies in Sweden, offering rental apartments for everyone, regardless of income, origin and age. The companies are professional with an active social responsibility.
[7] A planning document stating how a limited area in a municipality is to be built on and how land and water areas may be used.

(3) SBB has a wide financing base that consists of equity, bonds, hybrid bonds, commercial paper and just a small fraction of bank loans (SBB, 2019c). A fundamental strategy to optimize the capital structure with regards to credit rating is avoidance of pledging assets, instead focusing on unsecured financing from multiple bond markets (Batljan, 14.10.2020). *"Ilija's philosophy from the start has been important, namely, to be independent of banks and as quickly as possible enter the bond market to access unsecured financing"* (Schuss, 16.10.2020). The trend towards unsecured borrowing is also driven by relatively low rates in the bond market compared to secured bank loans. Finally, a key component related to both capital structure optimization and growth has been non-cash acquisitions (Johansson, 19.10.2020).

(4) Successful non-cash acquisitions have been decisive for the rapid growth to establish SBB, which requires the company to be listed on the stock exchange (Schuss, 16.10.2020). This strategy has implied a flat or growing equity ratio after each acquisition, facilitated by instruments such as D-shares and hybrid bonds (Johansson, 19.10.2020). SBB has three main share classes (A, B and D), where the non-tradable A-share has more voting power (SBB, 2019a). See Appendix 10.7 for shareholders and share characteristics. On the flip side, non-cash acquisitions cause dilution of ownership. However, as the largest shareholder, Batljan has not resisted dilution, which has enabled SBB to strengthen the equity ratio despite intense transaction activity (Johansson, 19.10.2020). *"I have never been afraid to dilute my ownership. Just ask yourself. Do you want to own a gas station, or do you prefer to own Shell? I always prefer Shell."* (Batljan, 14.10.2020). Worth mentioning is also that SBB has pursued non-cash acquisitions although the share has likely been undervalued. The reason being the importance to prepare the company for unsecured financing and building scale (Batljan, 14.10.2020).

(5) Scale is ultimately the key in real estate. First, the credit rating is likely to improve with scale and diversification, which decreases financing costs. Second, it enables the company to be listed and thus getting access to capital. Third, it creates an equity story towards counterparties (Johansson and Lekander, 19.10.2020). *"We have scaled our portfolio based on one mindset. If you own one property, the risk is huge. If you own ten properties, the risk is still large. But if you own 1,000 properties, the risk basically vanishes. A 0.1 percent effect on your balance sheet is nothing."* (Batljan, 14.10.2020). The platform of people enables scalability in SBB through specialized teams working together to benefit from all potential aspects of a transaction, such as kind of property and contract, potential renovations, ability to develop building rights, untapped land and possible surrounding properties to merge with (Batljan, 14.10.2020). *"We have a platform-based and scalable organization. The craftmanship is still the same if the transaction involves 10bn or 10mn."* (Batljan, 14.10.2020).

Growth journey (April 2016 – September 2019)

The business model has entailed a strong acquisition-driven growth. By Q3 2019, SBB possessed a SEK 30.8bn property portfolio, built from scratch in less than four years (SBB, 2019c). This section outlines significant events from the growth journey.

Figure 5

SBB portfolio development (Q4 2016 – Q3 2019)

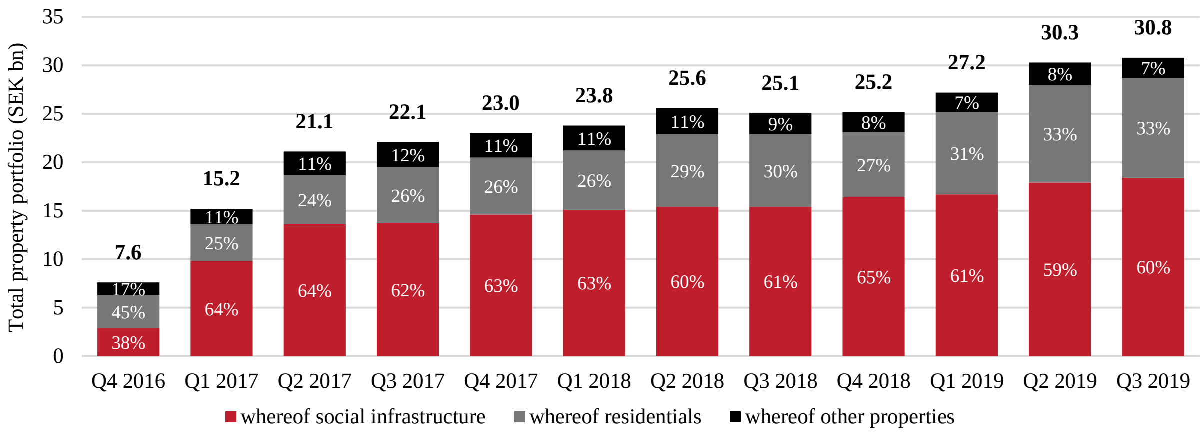


Figure 6

SBB average cost of debt development

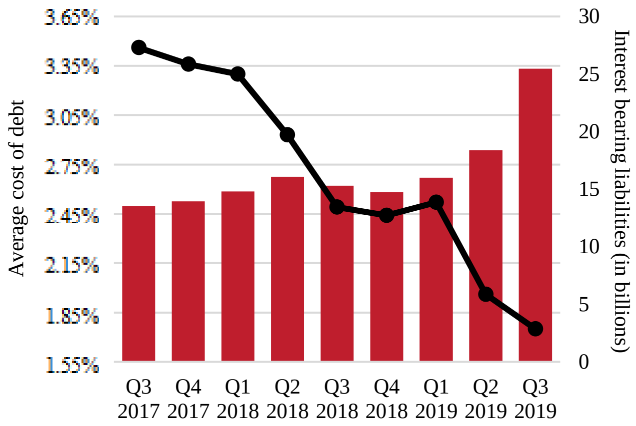
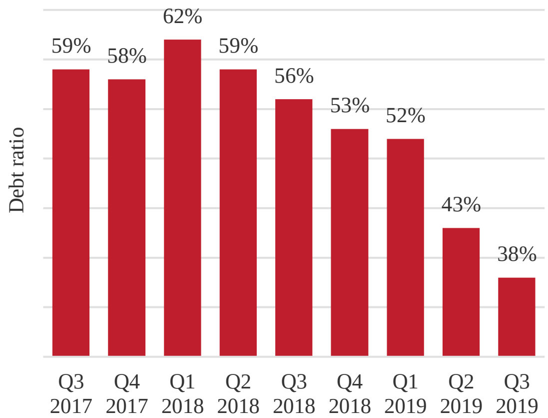


Figure 7

SBB debt ratio development



Source: Authors, SBB company reports

(2016) SBB was founded on March 2nd and already on April 1st the company acquired its first property, an elderly care home in Örkelljunga (Batljan, 14.10.2020). Even though the strategy is to focus on residentials and social infrastructure, initial transactions where in various sectors since higher yielding properties where essential to support a high cost of capital. Thus, successful transactions regardless of sector were important to achieve growth and a compelling equity story (Lekander, 19.10.2020). In September, SBB issued SEK 860m in equity, across ordinary shares, preference shares and convertibles to finance the acquisition of the Norwegian Ministry of Justice building, the seed asset in Norway (Fastighetsvärlden, 2016b). *"This deal gave us credibility in the market, as acquisitions in peripheral areas as Örkelljunga did not raise many eyebrows"* (Batljan, 14.10.2020). A month later, as previously mentioned, the owners of Gimmel Fastigheter joined SBB through a non-cash transaction. This was followed by a similar transaction on

December 5th with Högkullen Fastigheter, at the time the largest private owner of LSS[8] accommodation in Sweden (Schuss, 16.10.2020). Already the day after, SBB signed an agreement to backdoor into the stock exchange (Nasdaq First North) through a reverse merger. The transaction involved Effnetplattformen, a listed software company, who acquired SBB and the fellow real estate companies Kuststaden and Sörmlandsporten, creating the listed company Samhällsbyggnadsbolaget. In conjunction, Effnetplattformen distributed the software business to its existing owners (SBB, 2016). *"It was important to list as early as possible. You must be on the stock exchange if you lack capital for expansion, as it allows you to pay with shares"* (Schuss, 16.10.2020). In summary, SBB had during its first nine months, acquired 358 properties with a value of SEK 7.6 billion and created SEK 647 million worth of building rights (SBB, 2016).

(2017) In March, SBB surprised the market when announcing the largest acquisition to date: DNB's head office building in Oslo, purchased for NOK 4.3 billion. *"We saw a spread in yields and rents between Sweden and Norway, where the rent for a similar asset in Stockholm was about twice what DNB was paying, and those assets are not for sale. In addition, DNB was A+ rated and backed by the Norwegian state"* (Lekander, 19.10.2020). Although it was an office building outside the scope, cash flows were indirectly backed by the state (Batljan, 14.10.2020). In November, SBB obtained its first credit rating, B1, from Moody's (SBB, 2017b). By the end of 2017, the company portfolio had grown to 747 properties, valued at SEK 23 billion (SBB, 2017a).

(2018) During the year, SBB focused mostly on strengthening the balance sheet, by divesting non-core properties, refinancing SEK 7bn of existing credit facilities and new issuance of hybrid securities, B- and D-shares (SBB, 2018a). In February, the company entered the Finnish market by acquiring three elderly care homes and hired Lars Thagesson as the company's COO (SBB, 2018b, 2018c). In March, as a step to establish an in-house asset management organization, SBB acquired Hestia Samfast AB (Lekander, 19.10.2020). *"Our asset management was constantly struggling to keep up with the intense transaction activity."* (Schuss, 16.10.2020). SBB closed the year with a BB credit rating from S&P and Fitch and a portfolio of 570 properties, valued at SEK 25.2 billion (SBB, 2018a).

(2019) Strengthening the balance sheet continued in the beginning of 2019, by several issuances of new equity. As a result, the company finally achieved an investment grade credit rating, attaining BBB- from S&P and Fitch. In May, the company entered the Danish market through an acquisition of six properties in the capital region of Copenhagen and Aarhus (SBB, 2019d). As a result, SBB had presence in the four major Nordic countries. During September, SBB class B and D shares where approved for trading on Nasdaq Stockholm Large Cap, despite the short track record and history. The main reasons behind passing the due diligence were a solid three-year track record, with transparent high-quality accounting and the credibility from an

[8] LSS = Law on support and service for disabled (*Swe: Lagen om stöd och service till vissa funktionshindrade*)

experienced management team (Johansson, 19.10.2020). At the end of the third quarter, the SBB portfolio comprised 842 properties with an average lease length of 7 years, valued to SEK 30.8bn (SBB, 2019c). Towards entering the fourth quarter, SBB communicated new financial goals to grow the property portfolio to SEK 55bn with a BBB+ credit rating by 2021 (SBB, 2019c).

5.2.2 Hemfosa

Business model and growth journey

Figure 8

Hemfosa portfolio development (Q4 2016 – Q3 2019)

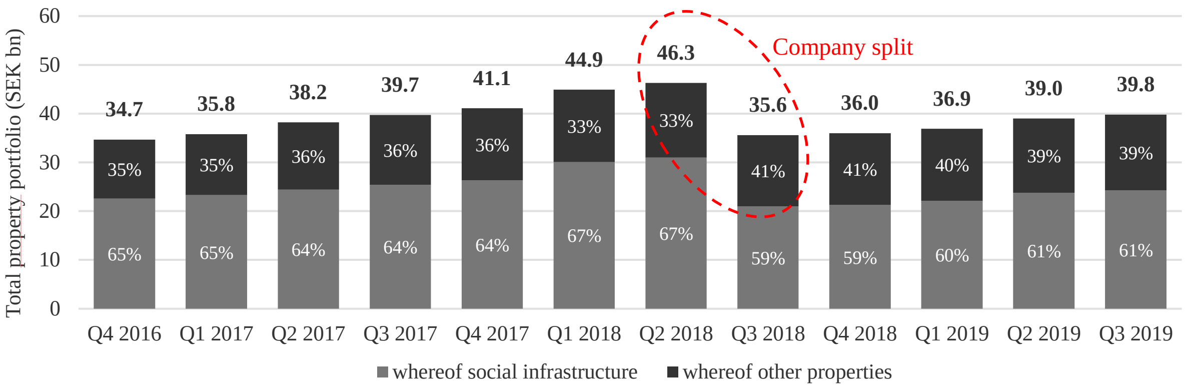


Figure 9

Hemfosa average cost of debt development

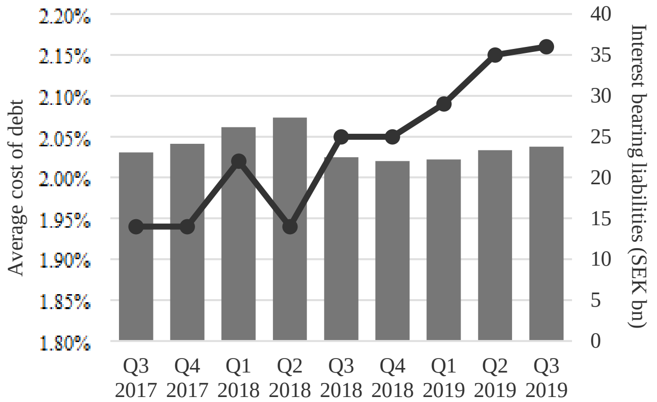
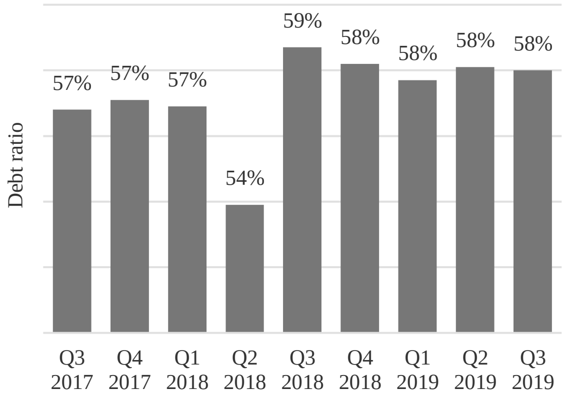


Figure 10

Hemfosa debt ratio development



Source: Authors, Hemfosa company reports

True to the wide shooting strategy, Hemfosa acquired office-, industrial-, warehouse-, care- and school properties in the first years of operation. Starting from scratch in 2009, the portfolio had in two years grown to 279 properties valued to SEK 15.1bn, through a series of insolvency related portfolio transactions (Hemfosa, 2014). *"We tried to limit the risk by having several smaller assets, no single asset could exceed 10 percent of the balance sheet and no single tenant contribute more than 10 percent of rental income."* (Thagesson, 28.10.2020).

As a condition from Hemfosa's institutional owners, the shareholders' agreement included an exit clause, where the company had to liquidate the portfolio or list it on a stock exchange by 2018. Therefore, in early 2013, the management team started to evaluate exit options. In the process, the team ended up settling for an IPO when market conditions seemed favorable. Hemfosa was eventually listed on Nasdaq Stockholm in March 2014, becoming the largest Swedish IPO in seven years (Thagesson, 28.10.2020; Fastighetsvärlden, 2014b). In connection with becoming listed, the business model was modified to actively focus on building a social infrastructure portfolio, as a complement to the opportunistic approach (Kjell, 10.11.2020). The shift towards social infrastructure came gradually to reduce risk and increase investor interest in the company (Thagesson, 28.10.2020). At the time, Hemfosa had built a property portfolio of 353 assets valued at SEK 27bn (Hemfosa, 2014) and the year after, Hemfosa entered Norway and Finland, becoming a Pan-Nordic real estate company (Hemfosa, 2015). In the following three years after the IPO, Hemfosa's social infrastructure portfolio grew to account for the majority of company revenue. As a result, the dual business model gradually became a problem, with two different types of businesses, commercial and social infrastructure, competing for resources. The opportunistic strategy implied intense transaction activity, where every asset was for sale at the right price, resulting in a high portfolio turnover. This left no reason for engaging in long-term initiatives such as development of building rights, which was common among industry peers. Therefore, in September 2018, the Hemfosa portfolio was separated into two specialized companies, allowing each business area to operate independently (Kjell, 10.11.2020). The split was carried out through a spin-off of the commercial real estate portfolio into a subsidiary, Nyfosa, that was distributed to existing shareholders. From this point, the "new Hemfosa" would solely focus on developing the social infrastructure business (Thagesson, 28.10.2020). Transitioning into 2019, Hemfosa had implemented a new business plan and communicated the intention to grow the portfolio from the current SEK 36bn to SEK 50bn within five years (Hemfosa, 2018a).

5.3 Case background

5.3.1 SBB end of 2019

By the end of September 2019, SBB had truly established themselves as one of the major real estate companies in the Nordics, with a unique portfolio among its listed peers combining social infrastructure and regulated residential properties. In addition, the company had reached one of its long-standing goals by attaining an investment grade credit rating, significantly improving access to financing by reaching a broader investor base (SBB, 2019c).

Figure 11
SBB portfolio composition Q3 2019

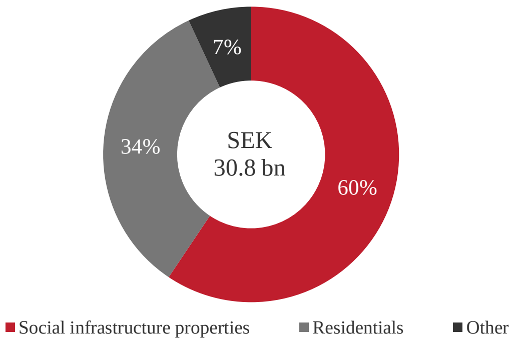
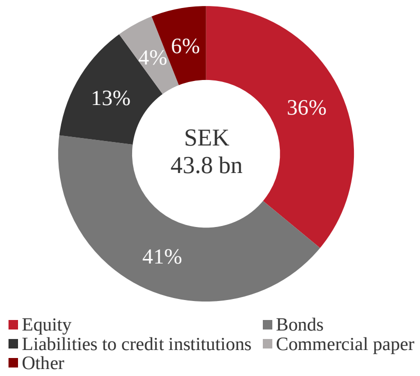


Figure 12
SBB capital structure Q3 2019



Source: SBB, 2019c

SBB had been active in capital markets with new debt and hybrid issuance totaling SEK ~17.2bn in the first nine months of 2019, borrowing at an average rate of 1.75 percent across the loan book (SBB, 2019c). Thus, accumulating around SEK 14bn in liquid assets available for new transactions, causing speculation of SBB's next move (Erik Penser Bank, 2019a). With the SBB shares approved for trading on Nasdaq Large Cap, equity also became a liquid currency for potential acquisitions (Lekander, 19.10.2020).

SBB had clearly signaled the intention to maintain a defensively positioned portfolio which implied a continuous focus on residential and social infrastructure properties, leaving very few realistic acquisition targets in the listed environment (Kaj, 16.10.2020). Additionally, SBB was determined to stay focused on growing in the Nordic home market and continue establishing a sufficient property management organization (Batljan, 14.10.2020). One potential target among few at the time was Hemfosa, a larger company with an attractive social infrastructure portfolio and an established property management organization. *"When I asked Ilija in the past if he would like to acquire Hemfosa he said that he indeed wanted, but needed to grow SBB and achieve a higher valuation before."* (Kaj, 16.10.2020). In parallel, SBB acquired a 20 percent stake, with an option for another 10 percent, in Amasten, a listed residential real estate company, led by Batljan's former Rikshem colleague Jan-Erik Höjvall, for SEK 711mn, prompting rumors of a buyout (Fastighetsvärlden, 2019a). A couple of days prior, SBB had purchased residential properties for SEK 1.5bn in cash from Amasten, and thus became the largest listed owner of Swedish residential real estate (Erik Penser Bank, 2019a). Simultaneously, the deal also involved creating a joint venture between the two companies, to develop new residentials on building rights purchased from SBB (Fastighetsvärlden, 2019b).

In terms of valuation, analysts from ABG Sundal Collier and Erik Penser Bank expressed positivity on the SBB share, by reporting a buy recommendation (Kaj, 16.10.2020), with a target share value 26.1 to 30.7 percent over the share price on October 30th. Together with SBB's track-record and growth targets, an EPRA NAV[9] premium was motivated (Erik Penser Bank, 2019a).

5.3.2 Hemfosa end of 2019

As a reshaped and niched company, Hemfosa had left the opportunistic business model, shifting focus on becoming a long-term player within social infrastructure. The new strategy further involved a greater focus on the customers and building a property development organization, which started to work actively with developing building rights on the back of the new long-term strategy. Towards the end of 2019, Hemfosa found themselves in a solid position. Both revenue, income and property portfolio were growing in line with the business plan and initial goals had all been achieved. However, there was still a need to continue building and strengthen the organization. In conjunction with the split back in 2018, a new management team had been put in

[9] EPRA NAV = European Public Real Estate Association's definition of Net Asset Value

place, focusing on structure and professionalization. *"Our management was quite inexperienced and unable to shift tempo. Although interest rates continued to fall, and cheap capital was available, we were not as fleet footed as our competitors to take the opportunity to do business. Instead, we stuck to our master plan."* (Kjell, 10.11.2020). Based on the opportunistic strategy previously operated by the "old Hemfosa" management before the separation, the company had built a reputation of being an active player in the real estate market. However, following the split and a revised strategy, the "new Hemfosa" was perceived relatively passive by the market. *"Hemfosa was not as active after the separation. It felt like they were burdened by internal processes, having a new organization and management in place, working with new strategies etc."* (Kaj, 16.10.2020). On the contrary, Hemfosa had a well-established, specialized and decentralized property management organization, which operated under strong independence. The organization included some 60 employees in total and each local team were responsible of the local business and customer relationships (Kjell, 10.11.2020).

Figure 13
Hemfosa portfolio composition Q3 2019

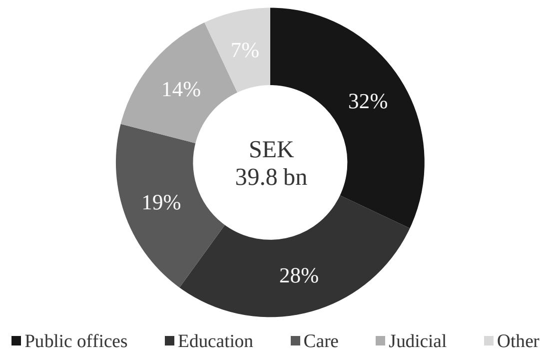
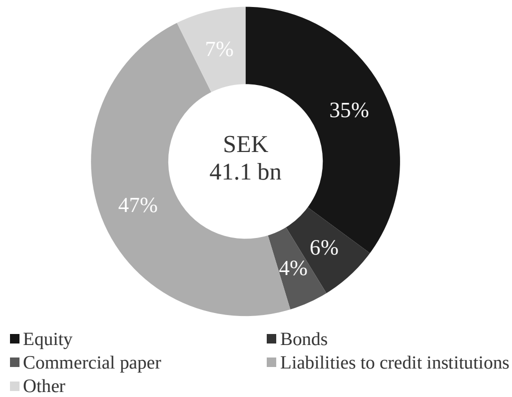


Figure 14
Hemfosa capital structure Q3 2019



Source: Hemfosa, 2019b

Despite the market's perception of a more passive Hemfosa, the portfolio was growing. By the end of September, the portfolio comprised properties to a value of SEK 39.8bn and had grown by approximately SEK 4bn during 2019, out of which SEK 2.1bn assignable to transactions. Acquisitions had been completed mainly in the Swedish market which composed the bulk of the portfolio (69 percent), but also in Norway and Finland which constituted 24 percent and 7 percent, respectively. At this point, Hemfosa communicated optimism with a strong acquisition pipeline and ongoing momentum (Hemfosa, 2019b).

The debt financing in Hemfosa mainly consisted of bank loans, and combined with minor capital market issuance, the average interest rate amounted to 2.16 percent across the loan book (Hemfosa, 2019b). The strategy ignored the credit rating aspect and had been used since the start of Hemfosa, based on the management's experience from previous success with Kungsleden prior to founding Hemfosa. *"There are different philosophies in financing. We have always worked with secured bank financing, which gives us a simpler, more straight forward strategy."* (Kjell, 10.11.2020). On the equity side, Hemfosa was mainly owned by institutions, with nine out of the ten largest owners being Swedish and international institutions (Hemfosa, 2019b), such as Länsförsäkringar, Swedbank, ICA and Blackrock. Furthermore, the ownership structure was based on a dispersed principle, implying that all owners held stakes smaller than 10 percent (Kjell, 10.11.2020). Appendix 10.8 presents the ownership structure in Hemfosa at the time.

In terms of valuation, the Hemfosa share traded on a 17 percent premium over its EPRA NAV, which motivated a sell recommendation from SEB based on their target value 17 percent below the share price on October 25th, corresponding to a P/NAV[10] of 0.95x (SEB, 2019). Furthermore, the high loan-to-value of 58 percent motivated a slightly higher cost of capital in Hemfosa (Carnegie, 2019). In contrast, ABG Sundal Collier had a more positive view on Hemfosa with a target value 14.9 percent above the share price on October 21st (ABG, 2019). In summary, analysts' recommendations diverged on the Hemfosa share.

6. The case: SBB acquires Hemfosa

This section narrates the acquisition of Hemfosa by SBB.

6.1 Preparing for an acquisition

As a transaction driven company, SBB was constantly evaluating the next opportunity and early concluded that a merger with Hemfosa would be the industrial dream. Already in 2017, the management team started to work on a structure that would make a deal possible (Schuss, 16.10.2020). *"It was incredibly important for us to build a large high-quality portfolio with a first-class property management organization. Hemfosa had both."* (Schuss, 16.10.2020). In conjunction, Ilija Batljan and Lennart Schuss approached Lars Thagesson, former COO and one of the founders of Hemfosa, offering him the position as COO in SBB. Batljan and Thagesson had become friends when both living in the same area outside of Stockholm and had during the years discussed the possibility of doing something together (Thagesson, 28.10.2020). *"I left Hemfosa with the intention to focus on my private business endeavors, forest and properties. But then, I spoke to Ilija a couple of years later about the idea to buy Hemfosa through SBB, and eventually I started working at SBB looking into that possibility. However, when we started pedaling, we were unsure if it was possible due to the size and many owners, including foreign institutions."* (Thagesson, 28.10.2020).

The road from idea to execution was not straight forward and SBB had much to work on to make a deal possible. After the Nyfosa spin-off, SBB began sounding towards Hemfosa, exploring interest in a potential transaction. *"When Hemfosa separated into two entities, we all obviously*

[10] Market capitalization divided by Net Asset Value

considered a deal. However, the discussions were not concrete, we probe multiple business opportunities every week. As a growing company, we are continuously looking at several companies." (Batljan, 16.11.2020). Even though the initial discussions did not result in any action, they revealed several major concerns of Hemfosa's owners to be addressed before a transaction could be considered. First, SBB was listed on Nasdaq First North, a multilateral trading facility operating with less regulation and disclosure rules (Nasdaq, 2019). Therefore, it was unthinkable for the institutional owners in Hemfosa to accept payment in SBB shares listed on First North, since they were equated to unlisted equity outside of their investment mandate. Secondly, Hemfosa made it clear that its shareholders would not consider a 100 percent equity offer, regardless of where SBB shares were listed. Finally, the two companies had vastly different capital structure philosophies, making it hard to find common ground on how to finance operations in case of a merger. For example, SBB had A class shares with high voting power, a significant difference to Hemfosa with only one class of common shares (Kjell, 10.11.2020).

Based on the premises, Hemfosa, the significantly larger company at the time[11] did not have an interest in pursuing a merger or bid for SBB (Kjell, 10.11.2020). SBB on the other hand, did not have the balance sheet nor capacity to finance such a transaction on a cash basis. Thus, the work continued for SBB to grow and build the financial capacity required to present a bid. Restrictions in the SBB share were evident, as listing on the main exchange was a prerequisite to use shares as part of the purchase price. In addition, the share price had to reach a certain level to avoid extensive dilution for existing shareholders (Schuss, 16.10.2020; Lekander, 19.10.2020). Eventually, in the summer of 2019, SBB's share price skyrocketed, appreciating by ~67 percent from June 28th to September 30th (Appendix 10.9), and the shares were approved for trading on Nasdaq Large Cap on September 20th (SBB, 2019c). Suddenly, SBB was in a financial position to consider submitting a bid (Schuss, 16.10.2020). Meanwhile, the team had several investment opportunities available. One being to use the existing toehold to proceed with a buyout of Amasten (Lekander, 19.10.2020). However, as a result from the appreciated share value and entrance on the main exchange, SBB had the ability to consider larger acquisitions. Therefore, Amasten was immediately put aside to allocate resources on the Hemfosa deal (Schuss, 16.10.2020). In addition, the team did not consider geographic expansion outside the Nordic market, further limiting potential takeover targets (Batljan, 14.10.2020). Consequently, Hemfosa was the obvious target for SBB, and clearly the best option available (Lekander, 19.10.2020). *"We had to decide what was best for our shareholders, acquiring Amasten or Hemfosa. Obviously, we chose to proceed with Hemfosa."* (Thagesson, 28.10.2020).

[11] At year-end 2018, Hemfosa's property portfolio comprised 381 properties valued at SEK 36.0bn, in comparison to SBB with 570 properties valued to SEK 25.2bn. (Hemfosa, 2018; SBB, 2018a)

6.2 The transaction

In mid-October 2019, SBB resumed contact with Hemfosa to further discuss a potential deal (Kjell, 10.11.2020). This process started one year after the Hemfosa split and around one and a half years after the Hemfosa founder, Lars Thagesson, had joined SBB. Based on the experienced management team in SBB and particularly Thagesson's detailed knowledge of Hemfosa, the following process would turn out to be relatively limited, short and intense for both parties (Batljan, 14.10.2020; Kjell, 10.11.2020). *"The sharp process lasted during the last ten days."* (Batljan, 16.11.2020).

Given the focus on financial stability and credit rating, SBB had spent substantial resources on preparations before presenting the proposal (Schuss, 16.10.2020). In fact, this preparatory phase was mainly an optimization exercise, in order to safeguard the credit rating and in tandem minimize the dilution effect for SBB shareholders, while still presenting an attractive bid (Batljan, 14.10.2020). Besides the work to optimize the bid structure, SBB evaluated Hemfosa's property portfolio both in terms of valuation and future potential through under-cover site visits and analyzes. This process was conducted with high precision thanks to the knowledge possessed by Thagesson (Thagesson, 28.10.2020). *"Lars Thagesson had probably been involved in acquiring most of the Hemfosa property portfolio"* (Kaj, 16.10.2020). The work involved an assessment of yields and external valuations as well as compatibility with the SBB portfolio for all the properties in Hemfosa's books, including the respective potential for developing building rights. *"Based on our analysis of the Hemfosa portfolio, 70 percent was both an incredible fit and, in our opinion, mis-valued. Although the remaining 30 percent were good cashflow generating properties, they were outside our scope. However, we could always sell those."* (Batljan, 14.10.2020). Furthermore, the process was facilitated by a transparent Swedish real estate system, which provides detailed information such as property ownership, location and size (Lekander, 19.10.2020). All in all, the extensive work involved the financial advisors JP Morgan, ABG Sundal Collier and Nordea, the legal advisors Vinge and Clifford Chance and a close cooperation with the credit rating institutions (SBB, 2019e).

When the stage was set and SBB had reached out to Hemfosa, discussions evolved mostly around the level of the bid and its composition, to make an attractive offer that shareholders in Hemfosa would be likely to accept (Batljan, 16.11.2020; Kjell 10.11.2020).

6.2.1 Initial proposal

Following the listing of SBB shares on Nasdaq Large Cap, Batljan contacted Kjell in mid-October 2019, presenting the interest in acquiring Hemfosa (Kjell, 10.11.2020). *"One element of the process was to first consider if a deal was in question at all, which later evolved into negotiations on price."* (Batljan, 16.11.2020). Although Hemfosa had previously pointed out critical standpoints and important aspects, SBB's initial probing was immediately dismissed by Kjell and the Hemfosa board. *"Ilija presented an idea of placing a bid, but it contained components of such nature that we immediately said, "No thanks". It was far too bad, both in terms of value and the composition."* (Kjell, 10.11.2020). Following the rejection, Batljan and SBB had to further concretize a more complete and attractive bid, including an optimal composition for the Hemfosa shareholders and proof of financing ability. *"Hemfosa saw the value for its shareholders to carry on their ownership in a larger combined company. Then, we had to consider the balance in the bid composition, to also enable cash consideration for those interested. However, the negotiation mostly involved finding an attractive price level."* (Batljan, 16.11.2020).

6.2.2 Negotiations

Shortly after presenting the initial proposal, SBB reverted with a well-prepared and financed indicative offer that was better received by the Hemfosa board, opening for a dialogue on key components. The indicative nature of the offer left room for negotiations before announcing a formal bid to the market. However, market abuse regulations put pressure on both parties to quickly reach an agreement. Therefore 2-3 days of hectic negotiations followed (Kjell, 10.11.2020). *"It was all about the value and the bid composition. The discussion barely involved integration and other administrative stuff. Hemfosa had recently been separated so the company was ready, thus it was all about the bid itself."* (Batljan, 14.10.2020). *"One cannot negotiate such a large deal in eternity. You must be prepared, ready to execute."* (Batljan, 16.11.2020).

Apart from that Hemfosa contested the total value in the previous offer, important parameters were the distribution between cash and equity, and optimization of legal and tax-technical aspects. First, one important element was the option allowing shareholders to select a desired distribution between cash and share consideration. Secondly, towards safeguarding the large tax exposure of its long-time owners, Hemfosa hired both legal and tax advisors. This collaboration resulted in a tax-optimizing component that was incorporated in the deal, which enabled the exchange of shares and the cash proceeds to be counted as two separate deals. *"This component was crucial for us in considering the shareholders' best interest."* (Kjell, 10.11.2020).

As a result of the discussions regarding value and composition, SBB presented a final revised offer to the Board of Directors in Hemfosa. With the parties being on the clock to reach an agreement, 7-10 days of final negotiations were carried out before SBB publicly announced the takeover bid (Kjell, 10.11.2020).

At first glance, Hemfosa found the final offer attractive. However, to carefully investigate the total value, they lined up with the financial advisors Swedbank, SEB and Handelsbanken. *"The hardest part of course, was to form an opinion on the value of the SBB shares that our shareholders would receive in return for tendered shares."* (Kjell, 10.11.2020). *"We had great collaboration. Our stock is very liquid, and we had recently done a rights issue."* (Batljan, 16.11.2020). The evaluation considered all key metrics, putting the value in relation to Hemfosa's share price, EPRA NAV, net operating income and growth projections, considering differences in the companies' liquidity affecting growth capacities. Hemfosa was fully invested at the time, whereas SBB had a large cash balance generated from previous financing activities leading up to the deal (Kjell, 10.11.2020). In parallel, Hemfosa and its advisors considered other potential Swedish, Nordic and European parties to seek a competing bidder, without anyone showing interest in presenting a comparable offer. Additionally, after taking into consideration the value of comparable firms and markets, the unanimous perception of the Hemfosa board and its advisors was that recommending the offer was in the shareholders' best interest (Kjell, 10.11.2020*). "SBB could have made a public offer earlier. In that case we could have worked on a different schedule in accordance with the Swedish takeover regulations. But SBB wanted to anchor the bid before going public."* (Kjell, 10.11.2020).

On the other side of the process, SBB had in turn presented two prerequisites in the final bid. First, the Hemfosa Board of Directors should support the bid before it was publicly announced, including an affirmative fairness opinion from an external advisor. *"We thought it was reasonable, given that they had negotiated a high price level, to demand that they should prepare a recommendation before announcement."* (Batljan, 16.11.2020). Secondly, SBB demanded conditions for conducting a limited due diligence (Kjell, 10.11.2020). In parallel with the ongoing discussions with Hemfosa, SBB had to consider how to convince large owners. As a first step, the night before announcement, SBB contacted Jens Engwall, the largest private owner and tenth overall, to inform that a deal would be announced the following morning. Engwall gave his consent and provided a recommendation for the bid to be included in SBB's bid prospect (Batljan, 16.11.2020).

6.2.3 Final bid announcement

After an intense negotiation and anchoring process, SBB on November 15th submitted a public offer to the Hemfosa shareholders. The offer valued the equity in Hemfosa to SEK 23,521mn, out of which SEK 21,380mn was assignable to the common share (SEK 126.15 per share) and the remaining SEK 2,141mn represented the preferred equity (SEK 193.63 per share), based on the closing prices of SBB Class B (SEK 23.85) and D shares (SEK 34.70) on November 14th (SBB, 2019e). Ex-ante, on November 14th, SBB and Hemfosa had market capitalizations of SEK 15,678mn and SEK 19,541mn, respectively (Eikon, 2020). The offer value implied a 22.7 percent premium for common shares and 1.1 percent for preference shares, corresponding to a 20.4 percent premium over the total market capitalization. Further, in relation to the substance value in Hemfosa, the offer corresponded to a 50.6 percent premium over EPRA NAV, based on reported values for the third quarter in 2019 (Hemfosa, 2019c; Eikon, 2020; Authors). Additionally, the bid composition offered a Mix & Match opportunity, whereby each of the Hemfosa common and preference shareholders could choose to receive share or cash consideration for tendered Hemfosa shares. The transaction was financed with 55 percent equity through issuance of new SBB Class B and D shares, with the remaining 45 percent to be paid with cash from the balance sheet backed by an acquisition finance facility. However, the offer did not contain guarantees in relation to bidder share price and the acceptance deadline for the offer was set to December 20th, 2019 (SBB, 2019e, 2019f). Table 4 below concludes the offer value for Hemfosa common and preference shareholders. For further details in the bid and its Mix and Match facility, see Appendix 10.10.

Table 4

SBB offer value to Hemfosa shareholders

Offer for Hemfosa common shares:

- in respect of 55 percent of the number of Hemfosa common shares tendered by such shareholder, 5.5 SBB Class B common shares per Hemfosa common share; and
- in respect of the remaining 45 percent of the number of Hemfosa common shares tendered by such shareholder, SEK 120.00 in cash per Hemfosa common share.

Offer for Hemfosa preference shares:

- in respect of 55 percent of the number of Hemfosa preference shares tendered by such shareholder, 5.6 SBB Class D common shares per Hemfosa preference share; and
- in respect of the remaining 45 percent of the number of Hemfosa preference shares tendered by such shareholder, SEK 195.00 in cash per Hemfosa preference share.

Source: SBB, 2019e

Immediately on announcement, the Hemfosa Board of Directors unanimously recommended the shareholders to accept the offer, noting that the value of share consideration under the Mix & Match opportunity would change over time (Hemfosa, 2019c). *"The deal rationale was logical, and the offer presented a value potential that was hard for us to accomplish on our own."* (Kjell, 10.11.2020). Combining the two companies would create the largest Nordic owner of social infrastructure properties and the fourth largest listed real estate company in the Nordics by asset value. The combined portfolio would total SEK 70.5bn in property value, generating SEK 3.5bn in net operating income. Further, SBB estimated that after-tax recurring synergies of SEK 300mn could be achieved, with SEK 260mn from financial cost synergies and the remaining SEK 40mn through operational cost synergies. The proposal highlighted additional value potential through development of building rights in Hemfosa's portfolio and scale benefits in renovation projects across the portfolios (SBB, 2019e). See Appendix 10.11 for a presentation of the combined entity.

In parallel, Batljan and his team instantly went out on a roadshow, both in Sweden and abroad, to start anchoring the bid among shareholders and large institutional owners such as Länsförsäkringar, ICA and Swedbank (Batljan, 16.11.2020). Against the background of SBB's recent acquisition of shares in Amasten, those holdings became part of getting consent. The transaction had namely resulted in almost erasing the shares' liquidity, causing anxiety among shareholders and personnel. With ICA and Länsförsäkringar also being large owners in Amasten, the shares held by SBB became a bargaining chip to gain support for the Hemfosa bid. Therefore, SBB undertook to divest the shares in Amasten. *"The owners demanded that SBB should leave Amasten in peace and prohibited them from acquiring Amasten in parallel to Hemfosa."* (Kjell, 10.11.2020). *"For us, the divestment of our holdings in Amasten was also a way to finance the bid for Hemfosa."* (Batljan, 16.11.2020). On December 4th, following the roadshow and associated negotiations, Länsförsäkringar and ICA publicly announced their support of SBB's public takeover offer (SBB, 2019j), later followed by Swedbank on December 19th (SBB, 2019k).

6.2.4 The acquisition process

Financing

A key consideration for SBB was the Hemfosa loan book, including change of control clauses, allowing creditors to terminate loan agreements and demand repayment in the event of major ownership changes (Schuss, 16.10.2020). "*We had prepared for the eventuality and had an approved SEK 30bn credit facility with JP Morgan. Including the cash on balance sheet it would have been possible to finance the transaction entirely with cash. So, we had been dry-swimming for a while securing funding sources. However, drawing down the facility would have ruined our credit rating*" (Batljan, 14.10.2020). As a step to finance the acquisition, SBB in parallel with the takeover offer launched a SEK 1.5bn rights issue directed to the company's existing shareholders, to support the joint business in attaining an investment grade credit rating. As a result, 65,443,061 new shares were issued at a subscription price of SEK 23.00 per SBB Class B common share, implying a 3.6 percent discount to the closing price on November 14th. In support of the rights issue, several members of the Board of Directors and company management committed to subscribe for shares and fully guaranteed the issuance (SBB, 2019f). *"If you sit on the board and want to carry out a deal like this, you think the deal is good. If something would happen, and we had to fulfill our guarantee, we were still convinced about the quality of the deal"* (Johansson, 19.10.2020). In addition, SBB listed SEK 1.5bn in subordinated perpetual callable notes in December, to further strengthen the balance sheet (SBB, 2019g). Finally, on December 18th, SBB notified the market of the disposal of their stake in Amasten for SEK 747mn, through an accelerated book building procedure (SBB, 2019h).

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A key milestone in the acquisition process was reached on November 26th when receiving clearance from the Swedish Competition Authority (Konkurrensverket, 2019). By the end of the acceptance period on December 20th, SBB had through tendered shares and parallel market purchases gained control of 87.1 percent of the shares and 88.1 percent of votes in Hemfosa, declaring the offer unconditional and extended the acceptance period to January 15th (SBB, 2019i). However, on January 17th, SBB announced that the acceptance deadline was further extended to January 29th (SBB, 2020e). After the final acceptance deadline had expired, SBB controlled 93.5 percent of the shares and 93.8 percent of the votes in Hemfosa. Thereafter, SBB called for compulsory redemption of the un-tendered shares. Finally, on January 31st, Hemfosa was delisted from Nasdaq Stockholm stock exchange (SBB, 2019a). See Appendix 10.12 for a complete timeline of events.

6.3 Deal motives

Given where SBB found themselves in the end of 2019, the acquisition of Hemfosa fulfilled several desired characteristics. The acquisition would namely generate considerable synergies and at the same time take SBB to the next level (Johansson, 19.10.2020). *"For us, Hemfosa was as close to Mona Lisa as it could get"* (Batljan, 14.10.2020). *"It was logical for SBB to grow substantially and we were the ultimate choice for them to achieve that. We also had a property management organization which they needed"* (Kjell, 10.11.2020).

Scale

First and foremost, the acquisition would more than double SBB's property portfolio by adding SEK 39.8bn to the existing SEK 30.8bn portfolio. By accomplishing this scale, plenty of positive side effects were expected. Generally, in relation to SBB's aggressive growth ambitions, such an acquisition took the company to an otherwise almost unreachable level and saved SBB tremendous amounts of time and effort in their growth journey (Lekander, 19.10.2020). *"To build a similar portfolio as Hemfosa's from scratch through small acquisitions is impossible for us. It cannot be done."* (Schuss, 16.10.2020). In addition, the Hemfosa portfolio comprised a vast majority of social infrastructure properties, which would make SBB the largest real estate company within social infrastructure in the Nordics (SBB, 2019a). Another key rationale related to scale was the effect on the credit rating, since size, which improves the diversification, is crucial when it comes to rating for real estate companies. *"The bigger you are, the better rating."* (Johansson, 19.10.2020). Mentioning diversification, the Hemfosa portfolio brought such advantages as well (Thagesson, 28.10.2020). SBB was namely heavily weighted towards the Swedish market, accounting for 83 percent of portfolio value (SBB, 2019c), whereas Hemfosa had almost SEK 10bn worth of properties in Norway, corresponding ~24 percent of its portfolio value (Hemfosa, 2019b). Consequently, the increased scale slightly re-balanced the combined portfolio, which enabled SBB to enhance its presence in both Norway and Finland while keeping the dominant position in the Swedish market (Thagesson, 28.10.2020). See Appendix 10.11.

Synergies

Secondly, the acquisition would generate distinct synergies. In total, the offer involved an annual synergy potential of SEK 300mn, out of which SEK 260mn was attributable to financial synergies (SBB, 2019e), due to relatively high financing costs in Hemfosa (Lekander, 19.10.2020). The average cost of debt in SBB was at the time 1.75 percent, compared to Hemfosa's 2.16 percent. Furthermore, Hemfosa fixed its cost of debt on an average duration of 2.3 years and tied its capital on 2.5 years, in comparison with SBB's 4.9 years (SBB, 2019c; Hemfosa, 2019b). In addition, SBB thought that Hemfosa had a suboptimal financing strategy mostly built on secured bank financing (Johansson, 19.10.2020). All in all, SBB felt confident about their financial expertise and ability to benefit from this comparative advantage, to create substantial synergies through refinancing activities (Batljan, 14.10.2020). The remaining SEK 40mn would come from operational synergies in the form of reduced overhead and streamlined property management (Lekander, 19.10.2020). For instance, the annual cost from being a listed company exceeds SEK 10mn itself, and therefore operational synergies were expected to exceed SEK 40mn in the long run (Kaj, 16.10.2020). However, synergies linked to property management and development potential, which involves value of building rights, were to a large extent left out of the synergy projection in the offer (Lekander, 19.10.2020).

Property management organization

Thirdly, the well-established property management organization in Hemfosa was one out of two main rationales behind the deal, together with the SEK 39.8bn portfolio (Batljan, 14.10.2020). The significance of this motive was explained by the constant struggle for SBB to continuously develop its property management business in line with the fast-growing portfolio (Lekander, 19.10.2020). Hemfosa's organization was specialized on social infrastructure properties, which would enable a smooth integration of the SBB portfolio into the Hemfosa management organization (Schuss, 16.10.2020). In addition, SBB prioritized to have the property management in-house, since joint ventures or outsourcing often comes with conflicting short-term incentives, which reduces the value potential (Lekander, 19.10.2020). Therefore, the deal was an optimal fit in this regard, by combining Hemfosa's property management with SBB's project development (Thagesson, 28.10.2020). *"Hemfosa was our dream. To combine our portfolios and access their property management was incredible. All pieces of the puzzle matched."* (Schuss, 16.10.2020).

Valuation and ownership structure

Finally, the timing of the acquisition was beneficial for SBB for several reasons. First, Hemfosa was considered a relatively easy takeover target at the time, following the effects from the recent split (Batljan, 14.10.2020). Hemfosa had ex-ante displayed an extreme transaction intensity over a long period of time, a strategy that almost ceased to exist after the split in favor of a more managerial role (Lekander, 19.10.2020). Hemfosa's recent passivity led to the second favorable motive, valuation, which seemed to suffer from lower activity in the company. Besides, Hemfosa was not as active in property development, leaving the value from potential building rights out of the balance sheet. *"I knew the company and that potential building rights were left out from their books, so we thought that there was more substance in the company beyond what was visible and appreciated by the market. Thus, we had to quickly initiate the process."* (Thagesson, 28.10.2020). Apart from the substance value, analysts who took an earnings approach in evaluating Hemfosa were indeed positive to the timing. *"The Hemfosa portfolio was attractively valued at the time* *given the quality and the cash flows it generated"* (Kaj, 16.10.2020). Further, the yields were expected to continue depreciating in the strong market, which made the portfolio more affordable for SBB (Lekander, 19.10.2020). The deal was also considered to be right in time based on the bid structure and the value of the SBB shares. *"When you could pay partly with shares valued well above your NAV, such an acquisition becomes great from many aspects"* (Johansson, 19.10.2020). Finally, Hemfosa had an ownership structure that would likely facilitate the deal-making. At the time, Hemfosa was namely driven by white-collar officials since most of the founders and large owners had made an exit (Lekander, 19.10.2020). *"Actually, Hemfosa had almost no owners that could block a takeover bid. Only a small fraction was owners of flesh and blood."* (Kaj, 16.10.2020).

6.4 Market reactions

Based on SBB's transaction intensity, growth ambitions and rumors from recent minority deals, the market anticipated further activity from SBB. However, when SBB announced the takeover bid for Hemfosa it came earlier than expected. *"Ilija had expressed this intention before, so it was logical. However, it was surprising that SBB already had the ability to acquire a much larger company than themselves. I thought it would take more time before SBB could bid for Hemfosa."* (Kaj, 16.10.2020). In fact, the deal turned out to be the largest Nordic M&A transaction in 2019 (Börskollen, 2020) and the all-time largest Nordic real estate deal (Fastighetsvärlden, 2019c).

Although the deal was somewhat anticipated, a few market participants, especially financial actors, did not understand the transaction. *"The market expected us to bid for Hemfosa. Lars Thagesson had recently joined SBB and we knew everything about Hemfosa. What the market questioned was our ability to finance the deal, involving possible bridge loans. But those who understood were extremely positive."* (Batljan, 14.10.2020). As a result, on the announcement day November 15th, SBB's shares reacted negatively, causing the B-share to drop by 8.2 percent and the D-share by 1.2 percent. On the contrary, the Hemfosa share reacted positively gaining 13 percent and the OMX Stockholm Real Estate Index appreciated by 0.95 percent (Eikon, 2020; Authors). *"The high premium was likely the reason why the market reacted negatively. We still paid 26-27 percent over the stock price and 50 percent over the substance value."* (Batljan, 14.10.2020). Finally, SBB had limited analyst coverage at the time and since ABG Sundal Collier, one of the few companies covering SBB acted as deal advisors, they were forbidden to write about the deal (Kaj, 16.10.2020). Finally, three days after announcement, for instance Erik Penser Bank reported a significant increase in their target value for the SBB B-share, corresponding to an average premium of 48.4 percent over the prevailing share price (Erik Penser Bank, 2019b).

Regarding the announced synergy potential of SEK 300mn, the value was in general considered reasonable. *"The synergies were fair. You could calculate the SEK 260mn financial synergies, and the remaining SEK 40mn is highly plausible when you have SEK 80bn in assets."*

(Kaj, 16.10.2020). As an example, at least SEK 90mn would solely come from the 40 basis-point-spread in average cost of debt between SBB and Hemfosa (Erik Penser Bank, 2019b).

6.5 Epilogue

After completing the takeover, SBB had to decide on composition of the new organization. Integration and merging cultures were foreseen as possible challenges that could result in a "we and them" mentality among employees. Initially, the SBB management team drew up a new organization chart to pick the best available team, resulting in the departure of around 30 overlapping personnel. The entire Hemfosa management team was made redundant, apart from Head of Property Management, Annika Ekström, taking over responsibility for property management in the new SBB organization (Thagesson, 28.10.2020). *"It is not possible to have two of everyone. Thus, we had to pick the best and it was not certain that the best belonged to SBB. We tried to build something like a football team, picking the best squad"* (Thagesson, 2020.10.28). As Hemfosa was already specialized on their own portfolio and social infrastructure properties, the integration turned out to be a smooth process that could be finished before the summer of 2020 (Schuss, 16.10.2020; Batljan, 14.10.2020).

After gaining control of Hemfosa, SBB signed letters of intent ("LOIs") to sell properties with a total value of around SEK 11bn, in accordance with the analysis of Hemfosa's portfolio with 30 percent of the properties being outside SBB's scope. The LOIs mainly concerned office properties from the Hemfosa portfolio with the proceeds to be used to repay bank loans, facilitating the company's ambition of attaining a BBB+ rating (SBB, 2019a). Following the outbreak of Covid-19 in the spring of 2020, Nyfosa that accounted for around SEK 8bn of the signed LOIs decided to postpone, causing headlines of a first major setback for SBB and Ilija Batljan (Fastighetsvärlden, 2020a). At this point, more unwelcomed news followed for SBB. On May 5th, Ilija Batljan was arrested, suspected of insider trading in conjunction with SBB's bid for Hemfosa. The shocking news put the SBB shares into free fall and the B share price plummeted by 40 percent, before closing 20.3 percent in red (SVT, 2020a; Eikon, 2020; Authors). However, Batljan was released the day after and all charges were dropped two weeks later (SVT, 2020b, 2020c). Despite a turbulent start of 2020, SBB had in June managed to divest properties for SEK 10.9bn in accordance with the disposal plan, involving a SEK 4.9bn transaction with Nyfosa. The divested properties were sold to an average premium of 15 percent over the reported values in Hemfosa (SBB, 2020a; Fastighetsvärlden 2020b). Refinancing activities, however, were initiated already in February when SBB announced repayment of SEK 10bn in secured bank debt. This refinancing was a first step towards the desired credit rating and generated SEK 170mn, out of the SEK 260mn, in financial synergies (SBB, 2020f). Those transactions started to build momentum for SBB, making the share appreciate by 34.7 percent in three weeks of February (Eikon, 2020; Authors). However, this quicky turned, due to the outbreak of Covid-19 and the announcement of a postponed deal with Nyfosa, affecting the overall perception of the Hemfosa deal (Batljan, 14.10.2020).

On August 21st, SBB announced that the remaining SEK 90mn in financial synergies would be realized, following repayment of all outstanding Hemfosa bonds and SEK 3bn of secured bank debt (SBB, 2020g). As a result, the full integration of Hemfosa was completed by the end of August. Refinancing and de-levering of the portfolio had been carried out and the communicated annual savings of SEK 300mn had been achieved, apart from an unexpected SEK 40mn accrual one-off attributable to tax-bound costs (Batljan, 14.10.2020). In conjunction, SBB presented updated financial targets to reach a BBB+ rating during the first half of 2021 and A- rating in the long-run, combined with ambitions of growing the property portfolio to SEK 125bn by 2025 (SBB, 2020b). As a step towards expanding the business, SBB launched a new business area, *state infrastructure*, venturing into specialized high security properties such as prison and military real estate (SBB, 2020c). In the third quarter of 2020, SBB reported a portfolio value of SEK 81.2bn with 94 percent allocation to social infrastructure and residential properties. The portfolio of building rights amounted to 2.85mn sq.m., equating to approximately 22,000 new apartments, which constitutes a platform for organic growth towards the new growth targets (SBB, 2020d). Appendix 10.13 presents the combined company portfolio and cost of debt as of 30.09.2020.

Although SBB owns and controls ~99 percent of Hemfosa, there is still an ongoing legal process regarding the compulsory redemption of the remaining outstanding shares. *"Neither the legal process nor minority shareholders affect us in running the company. The ongoing process is all about determining the price for minority's shares."* (Batljan, 16.11.2020).

"If we had not acquired Hemfosa, we would have experienced slower growth and needed more share issues. In addition to a hard grind to build the portfolio, it would have required work to strengthen the balance sheet to enable acquisitions. We would also have needed to focus efforts into building our management organization. Hemfosa contributed on all points, where we got a great property portfolio and a tuned-in management organization at once."

(Batljan, 2020.10.14).

7. Discussion

This section involves authors' analyzes and discussion on the results of this study in comparison with existing research. This mainly involves the growth journey of SBB and several aspects of the Hemfosa transaction such as deal motives and valuation.

7.1 A unique business model enabling growth

One cornerstone of this study is understanding the growth journey of SBB in the given real estate context. How is it possible to build a SEK ~80bn property portfolio from scratch in less than four years? What are the key success factors and decisive milestones? Is real estate somehow unique in this matter? The following section aims to analyze those questions, in which we will elaborate to what extent SBB's growth journey relates to existing research.

From a larger perspective, one can see that SBB's overall growth strategy has been three-dimensional, in line with Davis (2012) to enable maximization of shareholder value. SBB achieves *organic growth* through a dedicated property development organization, working on improvements and developing building rights from properties in the portfolio. Davis (2012) further states that *M&A* activity and *joint ventures* should depend on skillset, cash flows and targets, which is evident in the case of SBB. M&A has obviously been a fundamental driver behind building a SEK ~80bn portfolio, enabled by an experienced and proficient management dream team in the real estate sector. In addition, the relatively immature and fragmented social infrastructure segment has provided a substantial amount of target properties, which together with a privatization trend has paved the way for a M&A driven growth strategy. Also, following the high-intensity growth, SBB in the early stages entered several joint ventures to fill the knowledge gap in property development at the time, before establishing it in-house (Lekander, 19.10.2020). Besides, our study clearly displays that the achieved growth journey is derived from multiple sources paramount in the business model of SBB.

Social infrastructure and residential properties

The focus on social infrastructure and rent regulated housing has built a foundation of safe cash flows, on the one hand backed by the public sector over long durations and on the other hand indirectly secured from a severe supply deficit. Together with long-term ownership enabling value-creation from development of building rights, SBB's relatively low-rent strategy further creates stability since substitutes are almost non-existing, which ultimately mitigates properties' residual value risk. On the back of those characteristics, the company has become a key partner to the public sector in building societies' infrastructure, which in the end opens up for plenty of business opportunities essential for growth.

Wide financing base and credit rating

In combination with safe cash flows, the financing strategy with several share classes and a variety of instruments appears to be decisive in supporting the rapid growth. SBB has from the start strived to have a wide financing base, access unsecured financing and get a credit rating as quickly as possible. This strategy is in line with Kisgen (2006), who argues that the credit rating aspect affects managers' decisions on capital structure. Interesting to note here is that Hemfosa with a larger portfolio and higher market capitalization than SBB, ignored credit rating in favor of secured bank financing. One could hence see that both philosophies are applicable for large established real estate companies. However, we would argue that such fast growth as in the case with SBB demands for a wide financing base, to enable frequent large investments and to avoid higher cost of capital. Circulating back to the credit rating, Kisgen (2006) further finds evidence that firms on the edge to an up or downgrade in rating tend to issue less debt relative to equity. SBB confirms this theory since the quest towards investment grade has involved equity and hybrid issuances to continuously increase the equity ratio (Johansson, 19.10.2020).

Scale

Linked to financing and rating, we find scale to be crucial in real estate since it implies diversification between sectors, tenants and locations. *"[...] If you own one property, the risk is huge. If you own ten properties, the risk is still large. But if you own 1,000 properties, the risk basically vanishes. A 0.1 percent effect on your balance sheet is nothing."* (Batljan, 14.10.2020). Demirci et al. (2020) investigate this relationship, finding that lenders reward well-diversified real estate portfolios with lower lending rates. A review of Figures 5–6 clearly validates this theory, which also shows that debt becomes cheaper with size, in line with the analysis of Morri and Cristanziani (2009). Furthermore, as mentioned, the transaction driven growth has been crucial to build scale. In relation, Whittington et al. (2020) argue that acquisitions enable bidders to avoid spending resources on R&D by acquiring proven businesses. With regards to SBB in real estate terms, the large acquisitions (Hemfosa in particular) have boosted the growth compared to similar organic growth through long horizons of development and value increases. In our opinion, SBB could also be compared to IT-platforms for instance, with similar ability of scaling the operation, in this case based on the platform of people. To elaborate, the business model shares similar characteristics as asset management, since acquired properties and portfolios are easily integrated into the organization without demanding much additional resources. *"[...] The craftmanship is still the same if the transaction involves 10bn or 10mn."* (Batljan, 14.10.2020). Scale indeed relies on deep pockets which motivated the rapid listing for SBB, to access capital and the ability to use shares as currency for transactions, in accordance with Celikyurt et al. (2010). Furthermore, SBB's growth strategy confirms another finding of Celikyurt et al. (2010), since SBB upon listing intensified its transaction appetite, supporting that stock market listings significantly impact firms' ability to conduct acquisitions. *"To become listed is the only way. You must be on the stock exchange if you lack sufficient capital for expansion, since you can pay with shares. Therefore, it was critical to get listed as quickly as possible."* (Schuss, 16.10.2020). More specifically, SBB became public through a reverse merger, which saved substantial amount of time and effort compared to a normal IPO, acknowledged by Brenner and Scroff (2004). However, one could discuss the related controversy, whether the quality of governance and earnings is affected by avoiding the rigorous IPO registration process. Although SBB had motives behind a rapid stock market listing, we would argue that the real estate segment itself implies qualitative cash flows and that SBB's goal to reach Nasdaq Large Cap should catalyze for those risks. When SBB finally entered Nasdaq Large Cap, passing the rigorous due diligence process, they were able to strengthen the currency (share) and credibility, which ultimately enabled the Hemfosa transaction (Johansson, 19.10.2020).

Non-cash acquisitions

"The only way to create large real estate companies is through non-cash acquisitions. Otherwise it is impossible." (Schuss, 16.10.2020). Interestingly with regards to non-cash acquisitions, the case shows that real estate seems to stand out from traditional M&A theory, in which such transactions are often discussed from a valuation perspective. Dong et al. (2016) find that bidders who prefer to pay with stock likely are overvalued in relation to the targets, affecting investment decisions, financing and transactions overall. Shleifer and Vishny (2003) concur that stock acquisitions are made by overvalued acquirers, which incentivize firms to become overvalued to enable acquisition with stock. On the contrary, SBB seems to have somewhat contradicting motives. Although we find that the share value appears to be sticky, SBB has prioritized to build scale through non-cash acquisitions despite a lagging substance value, likely resulting in paying with undervalued shares (Batljan, 14.10.2020; Lekander, 19.10.2020). Therefore, SBB seems to violate the findings of Myers and Majluf (1984), that firms refuse to issue equity at a perceived bargain although the investment is positive-NPV. Furthermore, SBB displays the importance to take the whole company to the next level through non-cash acquisitions, although the share has likely been slightly undervalued in the process. In relation, one should however contemplate around the signaling effect, since financial markets often equal share acquisitions with overvaluation. Based on our analysis, we find this as a potential partial factor in explaining the stickiness of the SBB share price, even though Campbell et al. (2001) show that valuation signal in stock acquisitions is not as strong for real estate companies. In addition, Womack (2012) highlights that payment of mostly stock is used in ~52 percent of real estate transactions, which further explains that non-cash acquisitions are common in the sector. Combining with importance of scale, we find that non-cash acquisitions are key to enable high-paced growth. Therefore, the benefits of growing with a sustainable capital structure seem to outweigh the focus on valuation

in non-cash acquisitions when issuing new equity in real estate. However, we note that SBB expressly states that the share value had to increase to enable the Hemfosa transaction, which in some way follows the fundamental argument by Shleifer and Vishny (2003). On the other hand, it seems to have been more about reaching a fair value level thus not becoming overvalued. This analysis is further backed by analysts, with target values way above the prevailing SBB share price ex-ante (e.g. Erik Penser Bank, 2019a). Expanding towards dilution, it has interestingly been subordinated in the growth journey. However, the different share classes, with A-shares having more voting power, the dilution has been narrowed down to capital dilution while keeping control of the company. This has enabled substantial equity issuances without too much dilution of control. In summary, as stated by Kim and Canina (2015), managers involved in M&A are motivated by value creation. SBB confirms this theory but faces a dilemma. On one hand, the importance of building scale to exploit benefits from the rating-based financing strategy. On the other hand, being forced to use undervalued shares non-cash acquisitions to rapidly build scale (Batljan, 14.10.2020; Lekander, 19.10.2020). Consequently, one could ask why it has been so important to grow rapidly, when SBB had reason to believe their share was undervalued. Apart from strategies in the business model, we would argue that the fast growth has been driven by favorable timing to exploit market conditions with falling yields and all-time low interest rates.

7.2 M&A in a real estate context

From a structural perspective, we find the real estate industry well suited for acquisition-driven growth. With limited ability to grow organically, in combination with significant benefits from scale, real estate companies turn to M&A for growth. Additionally, the sector benefits from structural factors mitigating risks related to integration, recognized by Weber et al. (2013) as a key factor impacting the level of success in M&A transactions. In the context, acquisition of properties to an existing real estate portfolio is a pure asset transaction. Further, M&A involving real estate companies should also pose integration advantages since real estate business models require few employees, reducing challenges when merging organizations. As Figure 2 shows, transaction activity in the sector has steadily increased since the beginning of the millennia, displaying signs of a Nordic real estate merger wave, supported by improved access to capital and falling interest rates, a crucial factor for the capital-intensive real estate business. "*A prerequisite for a real estate market to develop is that the interest rate level is low.*" (Johansson, 19.10.2020). The pattern aligns with the broader findings of Whittington et al. (2020), that M&A activity is linked to stock market performance, availability of finance and the supply of target firms. In relation to supply, the market is fragmented with an abundance of clearly defined and ringfenced assets, forming a large pool of potential acquisition targets. However, being a successful acquiror often implies being forced to constantly pay the highest price. On the contrary, as shown by

Womack (2012), real estate mergers generally create wealth, where transactions are driven by firms with superior management acquiring targets with unexploited opportunities.

7.3 Hemfosa: SBB's Mona Lisa

"For us, Hemfosa was as close to Mona Lisa as it could get" (Batljan, 14.10.2020). This section scrutinizes relevant aspects behind this so-called "Industry dream", by analyzing components such as deal rationales, financing, bid composition and valuation, in relation to existing research.

7.3.1 Establishing a real estate giant

With regards to the fundamental form of the transaction involving SBB and Hemfosa, we find several aspects to address. As mentioned, *horizontal* and *vertical* deals are common forms of M&A and involves different rationales and potential synergies (Weber et al., 2013). Interestingly, SBB's acquisition of Hemfosa displays a combination of both horizontal and vertical motives, a deal structure which to a large extent is excluded in the selected theories. On the one hand, the deal is clearly horizontal since SBB and Hemfosa operate in the same industry. The transaction exhibits elements related to the *Monopoly theory*, as the combined entity significantly gained market share, market power and reduced competition in the social infrastructure segment, by becoming the fourth largest real estate company in the Nordics (see Appendix 10.11). In relation, we find a striking horizontal rationale, namely that the deal included a strong diversification motive, which according to theory rather is related to vertical deals. On the other hand, the rationale to access Hemfosa's property management organization aligns with forward vertical integration motives, since it could be viewed as a "distributor" to the property portfolio itself. Further, we find the vertical integration motive as two-dimensional, since Hemfosa from their perspective could benefit from SBB's established development organization. In line with Weber et al. (2013), the vertical motive becomes evident based on the smooth integration and focus on coordinating the SBB portfolio and Hemfosa's property management organization. Additionally, both forms of M&A are associated with different potential synergies, discussed in Section 7.3.2.

Furthermore, the deal can be analyzed based on the *Empire building theory* (Trautwein, 1990), where we identify contradictions between the case and existing theory. First, Berk and DeMarzo (2013) state that managers seek prestige in running large corporations and thus being likely go through with value-destroying investments to increase size. In contrast, both the real estate industry and SBB clearly show that becoming large is rather paramount in a real estate business model. Further, we find evidence to support Baker et al. (2012), who state that markets react more negatively on announcement involving bidders with past superior performance, since the SBB B-share dropped by 8.2 percent on the announcement day (Eikon, 2020; Authors). However, we identify the drop on announcement to mirror that the market equated the cash and equity offers, pushing SBB's share down to par with the cash consideration in the takeover offer[12].

In addition, we identify a conflict between our study and the *Process theory* (Trautwein, 1990). SBB extends this theory by proving that simplifications (e.g. limited due diligence) in the acquisition process were possible based on the deep understanding of Hemfosa's portfolio, rather than lack of information processing abilities. Further, SBB spent significant amount of time and effort in preparing the acquisition, which contradicts with the argument put forward by Whittington et al. (2020) that over-optimism causes managers to place irrational bids. However, one could identify signs of hubris and some over-optimism since SBB as a young company placed a bid on the significantly larger company, Hemfosa. But on the other hand, without the negative outcomes discussed in existing theory.

In summary, the transaction is considered successful from the following general angles brought forward in existing research. First, SBB's rigorous preparatory phase, involving valuation of each Hemfosa property, aligns with Gaughan (2005) and mitigated the risk of overpaying. Also, the visible and clear-cut synergies implied a solid valuation of the deal as a whole. Second, in line with Davis (2012) and Clark and Mills (2013), SBB carefully planned the integration process by identifying which properties to keep and those to divest and also outlined the strategy of refinancing, to achieve communicated synergies. Together, this enhanced the ability to attain the full value from the deal and in the combined company going forward, exemplified by realization of all communicated synergies merely seven months after gaining control of Hemfosa.

7.3.2 Substantial deal synergies

Synergies are often highlighted as the main incentive for M&A overall (Weber et al., 2013), with value creation achieved through utilization of economies of scale, cost and revenue synergies. Although financial synergies from a theoretical perspective should not exist in an efficient capital market, the Hemfosa transaction clearly supports the prevalence of, and ability to realize financial synergies, in a real estate context. In line with existing theory, that companies are awarded by lenders for increased size and portfolio diversification (e.g. Trautwein, 1990; Demirci et al., 2020; Morri and Cristanziani, 2009). However, the ability to achieve financial synergies also raises the question about capital structure choices in real estate companies. We note that SBB and Hemfosa before the merger adapted widely different philosophies in regard to capital structure, with SBB focusing on credit rating to access unsecured financing in capital markets, whereas Hemfosa favored secured borrowing in the form of bank loans. Consequently, we argue that such immediate financial synergies would be unachievable in a deal involving real estate companies with equivalent financing philosophies and cost of debt. The study suggests that the wider financing base available in international bond markets for investment grade rated companies indeed entails

[12] Cash offer SEK 120 divided by 5.5 SBB shares = SEK 21.82 (SBB closing price ex-post SEK 21.85)

access to lower cost capital, compared to what can be achieved for similar assets by unrated issuers or with traditional loan structures. Damodaran (2005) acknowledges that synergies are used to justify large premiums, noting that synergies are evasive concepts that are seldomly analyzed objectively. In contrast, our study shows that communicated financial synergies were visible and clear for market participants, by evaluating the spread in cost of debt between SBB and Hemfosa. More specifically, the synergy potential could be further analyzed by comparing terms on recent bond issuances for both companies. As an example, Hemfosa before the transaction issued bonds at a rate of Stibor 3M + 2.10 percent (Hemfosa, 2019b). To put this in context, SBB issued bonds with similar maturity at an interest rate of Stibor 3M + 1.20 percent (SBB, 2019c). However, the comparison is not straight forward due to the different underlying capital structures but serves as an indication in line with the findings of Baker and Martin (2011) on the credibility investment grade issuers have in the market. The emphasis placed on capital structure in the offer supports the evidence presented by Kisgen (2006), that credit rating considerations to a large extent affect manager's financing decisions, but also highlight that the rating was essential for realizing the estimated synergies. *"The entire bid was structured based on a calculation for what is required to maintain and improve our credit rating"* (Batljan, 14.10.2020). Furthermore, given that the Hemfosa debt portfolio mainly consisted of secured bank financing, one could question the reaction from SBB's existing bond holders, who partially became subordinated following the consolidation. However, as SBB communicated that financial synergies would come from refinancing Hemfosa's bank debt, we believe that the concern was likely negligible due to temporary subordination.

The realization of financial synergies, based on applying a different financing strategy, are in part attributable to what Trautwein (1990) describes as *Managerial Synergies*, when the target company's performance benefits from bidder managements' planning and monitoring abilities. This supports the findings of Womack (2012), that real estate mergers occur when acquirors with superior management find targets with unexploited opportunities to cut costs and/or increase revenues. Interestingly, SBB did not communicate any revenue synergies in the takeover offer, even though we note that SBB's building rights portfolio grew by approx. 700,000 sq.m., after the transaction, that converted to potential construction correspond to ~8,500 apartments (SBB 2019a; Authors). Although potential revenue synergies may have been difficult to quantify without proper due diligence, we interpret the absence of revenue synergies in the offer as a sign that SBB did not require additional synergies to justify the offer premium, in contrast with Damodaran (2005).

7.3.3 The Mix and Match bid composition

As mentioned, M&A theory states that overvalued bidders prefer to pay with stock in M&A transactions (Dong et al., 2016; Shleifer and Vishny, 2003). This would suggest that the Mix & Match offer to Hemfosa's shareholders meant that SBB was overvalued at the time. The argument is supported by SBB submitting the takeover offer after experiencing a share price rally in the months leading up to the transaction (see Appendix 10.9). Further, we note that the Hemfosa share traded below SBB's cash offer of SEK 120 per share during the first acceptance period, which could indicate that SBB was perceived by the market to be slightly overvalued at the time (see Appendix 10.9 for Hemfosa's share price development during the takeover period). However, we would argue that rather than pursuing an overvaluation, SBB was waiting for the share price to reach a fair value before the transaction. To elaborate, we believe that SBB's shares suffered from a liquidity discount while trading on Nasdaq First North, which could explain the share price rally when entering the main exchange since it opened for a broader investor base and strengthened the share currency. The fair value argument is further supported by members of the SBB Board of Directors and management team personally guaranteeing the SEK 1.5bn rights issue almost at par to the prevailing share price to finance the transaction. In addition, as previously mentioned, analysts reported target values significantly above SBB's share price ex-ante (e.g. Erik Penser Bank, 2019a), further defending the valuation of SBB.

Our view is rather that Hemfosa was relatively undervalued in relation to SBB. Looking at key metrics, the SBB offer posed a 50.6 percent premium over Hemfosa's EPRA NAV, significantly below SBB's valuation ex-ante, corresponding to an 81.9 percent premium over EPRA NAV. In relation, Hemfosa traded on a 22.7 percent premium to EPRA NAV ex-ante. (Eikon, 2020; Hemfosa, 2019b; SBB, 2019c; Authors). Also, we chose to analyse valuation from a cash flow perspective, showing that the offer valued Hemfosa at 15.6 times its cash earnings[13], in contrast to SBB trading at 36.1 times (Eikon, 2020; Hemfosa, 2019b; SBB, 2019c; Authors). The circumstances seem to align with the findings of Shleifer and Vishny (2003) that transactions involving share consideration are likely to occur when bidders have higher valuations relative to targets and the market perceives synergies from the transaction, although the bidder on a standalone basis might not have been overvalued.

7.3.4 Real estate valuation

In terms of valuation, real estate companies differ from other industries in how their assets are valued, with properties fair valued on a quarterly basis. The fundamental valuation methodology of a property's value implies discounting net operating income by an inflation-adjusted yield requirement. Thus, ignoring aspects such as capital structure, taxes and conventional valuation adjustments made for example in Free Cash Flow ("FCF") valuation. This ultimately implies that real estate companies are valued as a portfolio of properties, a fundamental difference compared to traditional valuation based on FCF growth forecasts. More specifically, real estate valuation tends to focus on properties' or companies' current substance value and operating income, rather

[13] Cash flow from operating activities before changes in working capital (As of 30.09.2019, last twelve months ("LTM"))

than complete longer-term growth effects derived from historical growth and annual investments financed by retained earnings. *"The substance value is more important in valuation of listed real estate companies than the cash earnings. In general, a premium to substance value is explained by expected value growth, and discounts are in general explained by expected decline in property values. However, I argue this does not capture the ability by management to over time generate growth and create shareholder value. If a company has reported a high and stable growth for a long period, I find it quite likely to assume continuous growth, but there is no correlation between earnings growth and earnings multiples in the real estate sector."* (Kaj, 16.10.2020). Further, the property valuation methodology is slightly backward looking, benchmarked to historical transactions (Kjell, 10.11.2020). As a result, realization of value changes becomes sticky, which in our opinion should tend real estate companies to be undervalued in a favourable market, since the company valuations are derived from the property portfolio value. The other way around, we see that the risk of overvaluation becomes probable in case of a market recession.

Interestingly, valuation methods differ among listed companies for how their most important asset values are reported. Some companies base property values on internal valuations whereas others rely on external consultants for valuation (Lindmark 23.10.2020; Kjell 10.11.2020). Given that companies have different approaches to valuation, we argue that direct comparison is too simplistic and requires more profound analysis. In this regard, we find that SBB and Hemfosa used the same methodology with independent valuers. However, the companies differed significantly in terms of reporting values of building rights, where SBB actively engage in property development and reports fair value on their building rights (SBB, 2019c). In contrast, Hemfosa was not as active in development and took a more conservative valuation approach. *"We were very careful with building rights because we did not work actively with development. We only valued building rights when there was a buyer for them."* (Kjell, 10.11.2020). All else equal, this implies that Hemfosa's property portfolio was undervalued in relation to SBB's.

Furthermore, assessing valuation of real estate companies seem to significantly differ depending on key metrics. Turning to Hemfosa on September 30th as an example, one can see that P / EPRA NAV[14] was in line with the peer group median, whereas P / CE[15] signals that Hemfosa traded on a 36 percent discount against the peer median (see Appendix 10.14.5). Such difference highlights the market's focus on substance value, which leads to another point of discussion. In the light of differing valuation methods, we argue that valuation based on substance values is unreliable. To elaborate, companies with the same NAV can still differ significantly in cash flows, which should be reflected in the valuation multiple due to different risk. The example above clearly violates this since Hemfosa's market value does not reflect the company's safe contracted cash flows. This suggests that real estate valuation should put more emphasis on earnings, since

[14] Market Capitalization to EPRA NAV
[15] Market Capitalization to LTM Cash Earnings

cash flows in the end also serves debt payments and dictates the ability to grow, and should thus dictate the valuation of real estate companies.

7.3.5 Undervalued target acquired at significant premium

Apart from the strategic aspects previously discussed, the case presents several signs that the Hemfosa share was undervalued. Both SBB and analysts explicitly state that the Hemfosa portfolio was attractively valued at the time, probably driven by the change in strategy following the split and conservative approach in valuation (Batljan, 14.10.2020; Thagesson, 28.10.2020). To exemplify, one could find evidence of undervaluation since SBB divested properties from the Hemfosa portfolio on a 15 percent premium over reported fair value (Fastighetsvärlden, 2020b).

Although Hemfosa was likely undervalued, the SBB offer represented a significant premium which not necessarily means that SBB made a bargain. However, SBB traded on multiples way above Hemfosa and significant synergies could be realized from the deal. Therefore, one must assess several factors when analyzing the level of the bid. Appendix 10.14 presents the authors' two-scenario valuation of Hemfosa, based on previously mentioned real estate valuation methodology. The first scenario excludes real growth potential, more aligned to conventional real estate valuation, generating a standalone value 2.8 percent above the prevailing share price on November 14th. This contributes to the sign of undervaluation, but also displays that the SBB offer at a 22.7 percent premium involved synergies and potentially a differing view of the standalone value. Therefore, our second valuation scenario takes real growth into consideration, in line with Hemfosa's business plan, generating a share value 17.9 percent above the prevailing share price. Still being below the 22.7 percent takeover premium, this further suggests an evaluation of the potential value from synergies, presented in Appendix 10.14.3. Our valuation shows an estimated value of communicated synergies around SEK 4bn (SEK 24.3 per share), which can be used in two ways in evaluating the SBB offer. On the one hand, given Hemfosa's share price on November 14th of SEK 102.8, the SBB offer of SEK 126.15 would have implied a transfer of almost the full synergy value to Hemfosa shareholders. However, we find it unlikely that SBB would give away almost the full synergy potential. Therefore, we argue for the growth case value of SEK 121.2 per share and assume this value as the fair standalone value of Hemfosa, supported by the SEK 120 cash offer from SBB. In connection with the bid composition, this enabled sceptics on SBB's share price to cash out the imbedded business plan value, and supporters would receive shares and thus subsequently benefit from the full long-term synergy potential as owners in the combined entity. In summary, the weighted SBB offer value in relation to our growth case valuation implies that an average of 20.5 percent of synergies were transferred to Hemfosa shareholders. All in all, we find the takeover offer value reasonable since Hemfosa likely received a considerable share of synergies on top of the full embedded value in the business plan. From SBB's point of view, apart from the discussed transaction motives, the absence of competing bidders was beneficial and likely enabled SBB to attain the majority of synergies.

In terms of key metrics, the takeover offer value appears expensive at first sight due to a 50.6 percent premium over Hemfosa's EPRA NAV, in relation to the peer group median of 17.3 percent and Hemfosa's prevailing 22.7 percent premium ex-ante (see Appendix 10.14.5). However, from the earnings approach, which was not communicated in the takeover offer, the deal corresponded to a P / CE multiple of 15.6x, well-below the industry median of 19.2x. One should question the fairness of a relatively low earnings multiple for Hemfosa, in relation to the safe contracted cash flows from the public sector and proven ability to grow annually from reinvested earnings with constant debt-ratio. As a result, one could argue that SBB's takeover offer was a bargain when analyzing the P / CE multiple, since the relevance of the EPRA NAV relies on accurate valuation of underlying assets, which evidently was not the case for Hemfosa.

Finally, we claim that the communicated financial synergies of SEK 260mn were not disclosing the full potential value in the combined entity. In fact, the deal synergies only involved refinancing of the Hemfosa portfolio, thus excluding the value from decreased cost of debt, achieved through increased scale and improved credit rating, for the combined entity in the long run. In summary, the deal involved substantial synergies without being stretched to the limit, since financial synergies in the combined portfolio and revenue synergies from building rights were not disclosed in the takeover offer. Therefore, we find the communicated deal synergies prudent, only including the most tangible cost savings from the deal.

8. Conclusions

Growth journey

The investigation of SBB's growth journey towards becoming a real estate giant in merely four years evolves around the following key success factors. First, non-cash acquisitions are a proven part of the company's DNA. We find the willingness to issue equity as the most important reason that SBB in a short period of time has been able to build the scale necessary to become an industry leader. Having two share classes with different voting rights from the start made it possible for SBB to grow through non-cash acquisitions and maintain solvency, without experiencing the same dilution of control usually associated with equity issuance. Secondly, the financing strategy based on credit rating and accessing a wide financing base in the bond market, has allowed SBB to maximize the benefits of scale to constantly shrink the cost of capital. Finally, a platform of experienced key employees has been crucial for the practical implementation of the strategy to achieve such astounding growth. In addition to a carefully outlined strategy, we acknowledge that SBB has benefitted from favorable timing, as market conditions have been positive in combination with rapidly growing demand for social infrastructure properties. We find that it would be nearly impossible to achieve similar growth in the real estate industry if not supported by low interest rates and readily available capital. On the back of building scale through non-cash acquisitions, SBB has ultimately succeeded in growing to one of the largest real estate companies in the Nordics, offering investors a unique product with similarities to a municipal bond with a spice of real estate development. The findings from our study of SBB's growth journey adds to existing research, mainly by providing evidence that non-cash acquisitions have not primarily been driven by overvaluation, but rather used as a tool for SBB to quickly achieve scale without over-leveraging, although the shares likely have been undervalued in the process.

Real estate valuation

We find fundamental differences in how real estate companies are valued compared to other industries and how real estate companies in turn value their assets. The findings suggest that real estate companies to a large extent are valued based on their existing portfolio and income, where future cash flow growth is excluded from the valuation methodology. Consequently, we argue that valuation of real estate companies should focus more on the earnings approach, a factor overlooked by the market today, as it ignores differences in companies' asset valuation methods.

The Hemfosa transaction

The acquisition of Hemfosa was the most important event of the growth journey, truly establishing SBB in the market. Most importantly, the deal would more than double, and thus diversify, SBB's property portfolio and offer a potential to generate substantial synergies. In addition, perceived undervaluation of Hemfosa's property portfolio is considered a key motive based on SBB's knowledge of the company. Although the deal was a horizontal transaction, we also find evident vertical merger motives in combining Hemfosa's property management organization and SBB's development franchise, complementing weaknesses in the individual companies. Furthermore, the differing capital structures and financing costs allowed the realization of approximately SEK 260mn in clear-cut annual financial synergies, by refinancing bank loans in the bond market. We also conclude that the Mix & Match bid composition allowed SBB to finance the deal while safeguarding the combined entity's capital structure to maintain an investment grade credit rating, essential to realize communicated synergies. Finally, we find the takeover value to be fair vis-à-vis the shareholders of both parties, although we note that the offer value still implied a discount compared to earnings multiples among comparable listed companies.

Suggested future research

First, we believe a study assessing the long-term value development of real estate companies with strong earnings development would be of great interest, to extend our finding that the market risks to systematically underestimate growth potential by ignoring earnings capacity in valuation. Secondly, real estate companies differ in how their assets are valued, opening up for further research to examine valuation practices in listed real estate companies. Thirdly, our study exhibits significant differences in real estate companies' capital structures. Thus, we find this interesting for future research both in terms of how capital structure choices affect the ability of real estate companies to grow and how alternative financing sources, such as preference shares and hybrid instruments, affect the overall cost of capital for real estate companies.

9. References

9.1 Interviews

	Interview date	Interviewee	Interview format
1	14 October, 2020	Ilija Batljan	In-person
2	16 October, 2020	Tobias Kaj	In-person
3	16 October, 2020	Lennart Schuss	In-person
4	16 October, 2020	Anonymous analyst	In-person
5	19 October, 2020	Oskar Lekander	In-person
6	19 October, 2020	Sven-Olof Johansson	Telephone
7	23 October, 2020	Ulrika Lindmark	In-person
8	27 October, 2020	Mats Gerdau	Telephone
9	28 October, 2020	Lars Thagesson	In-person
10	2 November, 2020	Samuel Lundqvist	Telephone
11	10 November, 2020	Bengt Kjell	Telephone
12	16 November, 2020	Ilija Batljan	Telephone

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10. Appendix

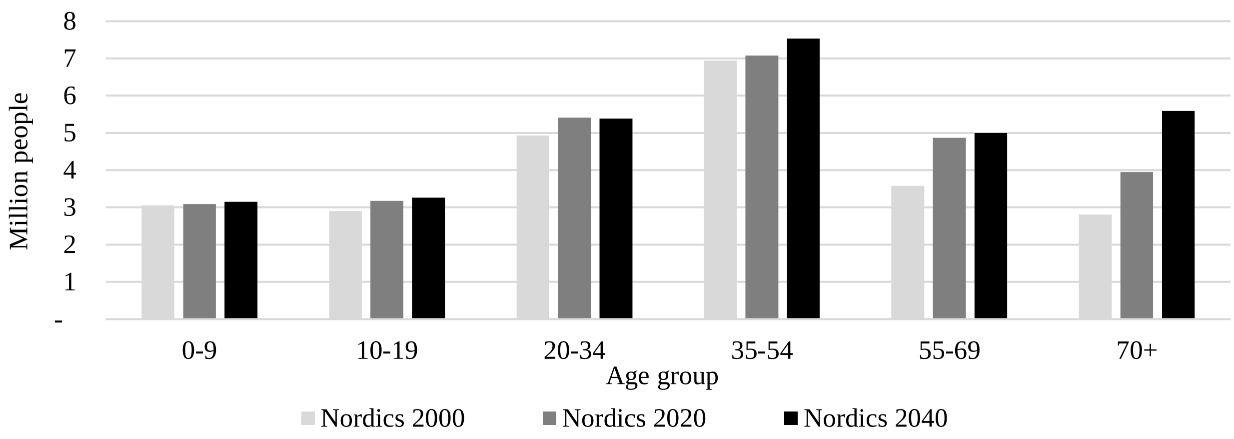
10.1 State interventions in municipal finances

	DENMARK	FINLAND	SWEDEN	NORWAY
Local government under stress	Municipality of Farum, (2002)	Municipality of Karkkilla, (1992)	City of Bjuv, (1995)	Municipality of Lebesby, (Late 1980s)
Background	Excessive spending and breaches of borrowing regulations. Several ambitious projects were carried out via opque public-private partnerships using sale and leasback loans.	Financial distress of a major state-owned company (Karkkila Industrial Village Ltd.) with domestic and foreign loans guaranteed by the municipality. A devaluation of the Finnish Markka exacerbated the situation, pushing guaranteed loans up to 250% of the municipality's tax revenue.	Financial distress due to the overindebtedness of its housing company. Bjuv was unable to raise taxes at the time due to nationa legislation that suspended municipalities' tax-raising powers.	The municipality guaranteed the liabilities of a fishing business that went bankrupt, and was forced to assume responsibility for NOK 50 million of its short—term debt.
State intervention	The central government assumed control of Farum and granted the municiality a subsidy of DKK 2 billion, a sum equivalent to its annual budget. This marked the first time the Danish central government had bailed out a local government, and was highly controversial in Denmark. Farum was forced to raise municipal taxes from 19.6% to 22.8%.	Karkkila took the liabilities on its balance sheet and the central government was given the right to veto the company board. The central government passed emergency legislation tha tenabled the payment of a state interest subsidy to the municipality, which had to be repaid. Karkkila raised municipal taxes to the highest level in the country.	The central government provided SEK 159 million out of the SEK200 million requested to resolve the crisis. It also took over the housing company until 31 May 2003 as a condition of allowing Bjuv to keep it thereafter. Bjuv took a larger management role in the housing company.	The central government provided financial support for number of years, and allowed the debt to be restructured as part of a wider rescue package that also imposed spending cuts and closer scrutiny on the municipality.

Source: Moody's 2018

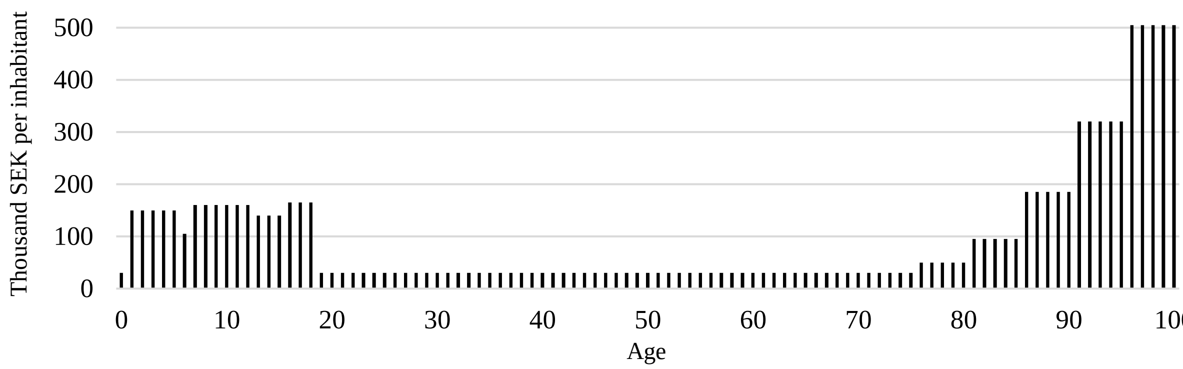
10.2 Nordic population forecast and cost per inhabitant by age

Nordic population forecast by age group (2000 – 2040)



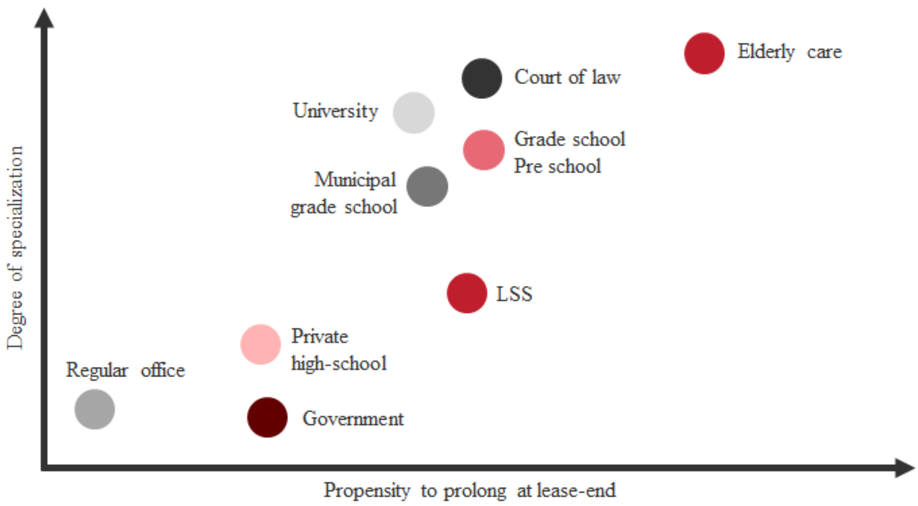
Source: Nordic Statistics Database

Cost per inhabitant sorted on age (2016)



Source: SCB

10.3 Assessment of tenant turnover



Source: SBB, 2019e (Newsec)

10.4 Rents and yields in the Nordics

Rents

Sweden			**Rent level**			
SEK/sq.m./year	**Elderly care**	**LSS**	**Health care**	**Education**	**University**	**Judicial sector**
Stockholm Prime	1700-2500	1500-3000	1500-3000	1600-3200	2000-4000	1700-4600
Gothenburg Prime	1600-2400	1400-2900	1300-2800	1300-2400	1100-2800	1500-3000
Malmö Prime	1500-2300	1300-2800	1200-2600	1200-2300	1400-2700	1300-2700
Other major cities	1100-2300	1200-2800	1100-2400	1100-2300	1300-2500	1200-2500
Rest of Sweden	950-2100	1100-2700	1000-2000	1000-2100	1200-2200	1100-2200

Norway			**Rent level**		
NOK/sq.m./year	**Office**	**LSS**	**Health care**	**Education**	**Judicial sector**
Oslo Prime	2000-3000	1500-3200	1500-3800	1300-2900	1800-2400
Tier 2 cities	1700-2800	1100-2500	1400-3600	1200-2400	1700-2200
Tier 3 cities	1300-2200	900-2200	1100-3200	1200-2200	1500-2000

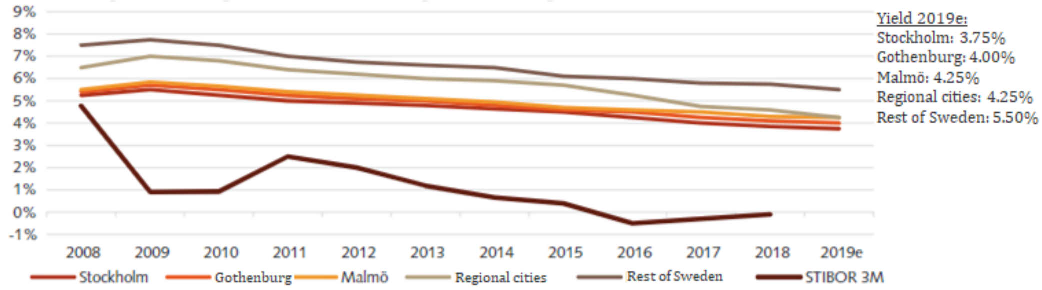
Finland			**Rent level**			
EUR/sq.m./year	**Elderly care**		**Daycare**		**Education**	
Large Helsinki	205-230	190-215	190-205	170-190	215-300	170-230
Tampere	190-215	170-190	180-205	145-155	190-240	130-190
Turku	190-215	170-190	180-205	145-155	190-240	130-190
Oulu	190-215	170-190	180-205	145-155	190-240	130-190
Jyväskylä	190-215	170-190	180-205	145-155	190-240	130-190
Others	180-205	120-180	180-205	110-145	170-205	120-180

Denmark			**Rent level**			
DKK/sq.m./year	**Elderly care**	**Senior housing**	**Health care**	**Education**	**University**	**Judicial sector**
Copenhagen	1375-2000	1375-2000	1000-1900	1400-2000	1400-1950	1300-1950
Aarhus	1125-1400	1125-1400	800-1300	1000-1300	1000-1300	900-1475
Odense	825-1225	825-1225	600-1100	600-1100	600-1100	600-1100
Other major cities	750-1100	750-1100	500-800	500-1100	500-1100	500-1100
Rest of Denmark	575-900	575-900	500-700	500-700	500-900	500-900

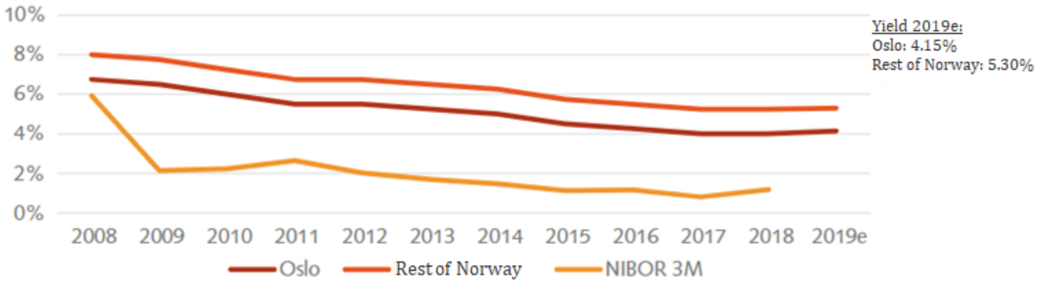
Source: SBB, 2019e (Newsec)

Yields

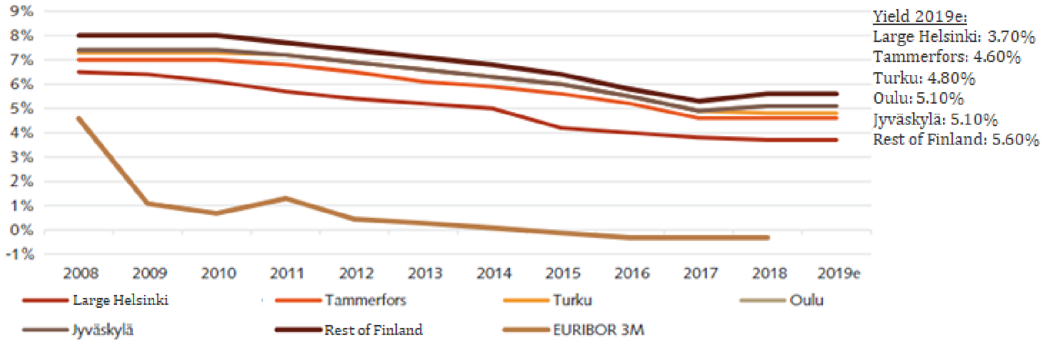
Yield development, all social infrastructure properties, Sweden



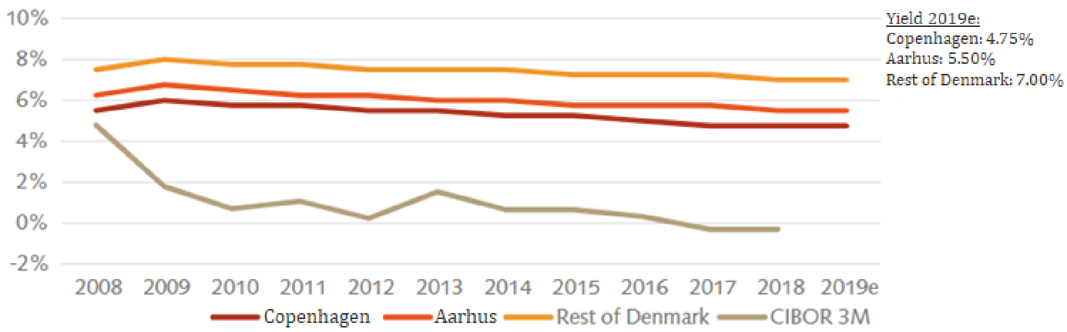
Yield development, all social infrastructure properties, Norway



Yield development, all social infrastructure properties, Finland



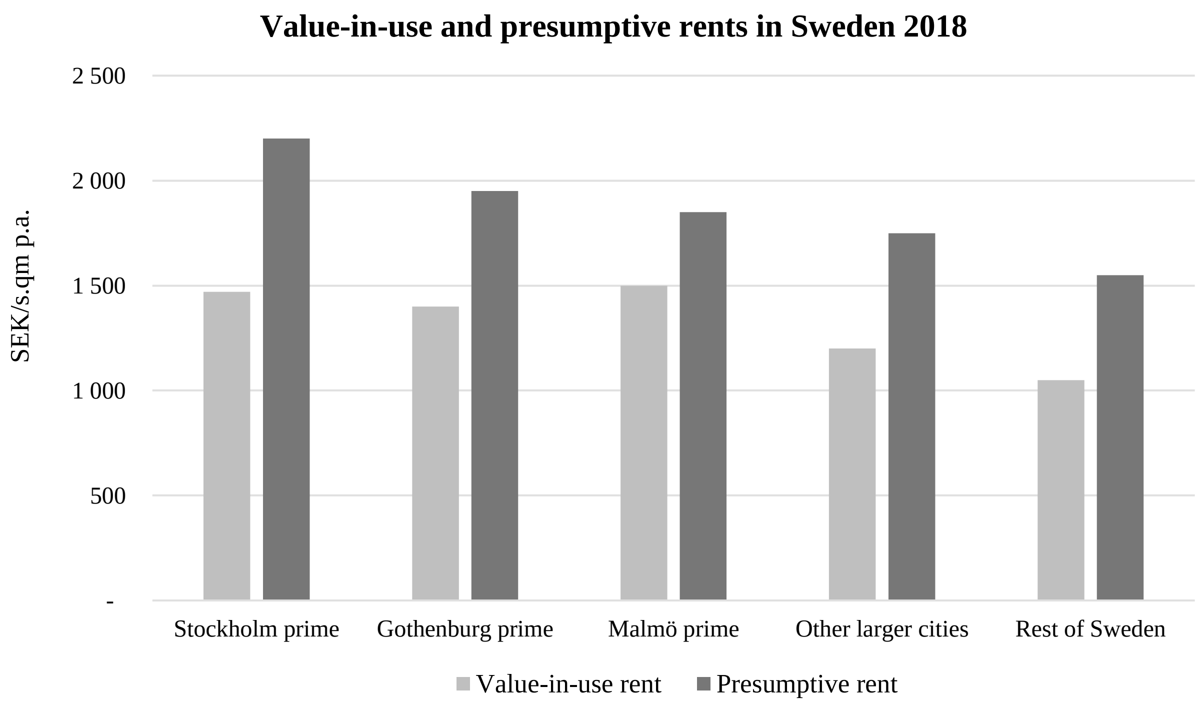
Yield development, all social infrastructure properties, Denmark



Source: SBB, 2019e (Newsec)

10.5 Presumptive rents

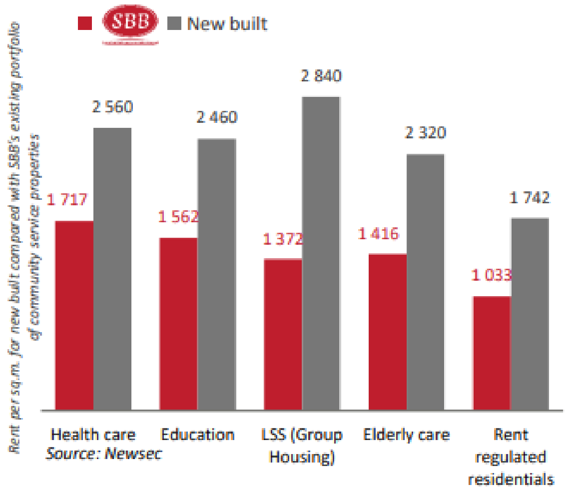
Rents in the older stock tend to be below market rent, at least in attractive areas, due to the value-in-use system. Apartments built after 2006 are closer to market rent as a result of different ways of setting the rent. In order to create incentives to build new homes with rental apartments, a new model with presumptive rents *(Swe: Presumptionshyra*) was introduced in 2006 (Jordabalk, 1970). The model for presumptive rents is based on the apartment's production cost instead of its value-in-use. The purpose of presumptive rent is to promote new construction of rental apartments by giving the property owner the opportunity to set a higher rent than the value-in-use-system allows. The presumptive rent is set at a level that covers the developer's construction costs and allows a profit margin in the project. Thus, these rents are more market oriented. Apartments with presumptive rents cannot be used as reference objects in value-in-use rent setting. Presumptive rents are also locked in for 15 years, meaning they cannot be tested for value-in-use or raised if the standard in the apartment is improved during this period. After the initial 15 years, rent setting transfers to the value-in-use system. Since the system was implemented in 2006, no apartments have yet been transferred and implications from a property owners' perspective are hard to evaluate. The difference between value-in-use rent and presumptive rent is often large, and this might have significant implications for property owners with presumptive rent contracts. The graph below shows an overview of differences in rents under the two systems.

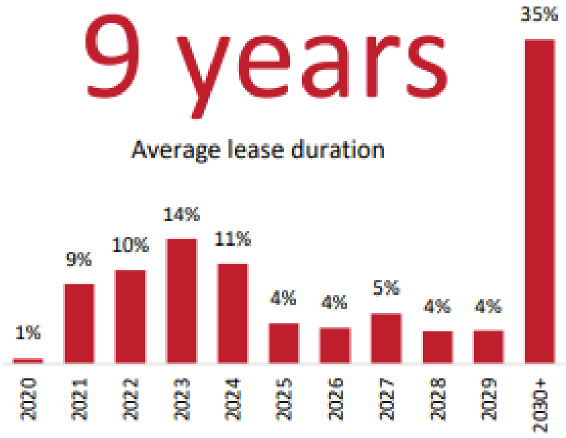


Source: SBB, 2019e (Newsec)

10.6 SBB – rent levels and average lease duration

As of 30.09.2020





Source: SBB, 2020d

10.7 SBB – ownership structure and share classes

As of 30.09.2019

SHAREHOLDERS

As of 30-09-2019, the share capital amounted to SEK 83,257,974 with a quota value of SEK 0.1. Being a shareholder entitles the right to vote at the Annual General Meeting with one vote per class A share and 0.1 vote per ordinary share of class B, class D and preference share. The preference shares have a preferential right over the ordinary shares to an annual dividend of SEK 35, paid quarterly, per preference share. Holders of the ordinary shares of series D are entitled to five times the total dividend on the ordinary shares of series A and B, however no more than SEK 2 per share and year. The largest shareholder is Ilija Batljan, who directly and indirectly holds 13.2 percent of the capital and 40.1 percent of the votes.

Shareholders	Amount Class A	Amount Class B	Amount Class D	Amount Pref. shares	Share of capital, %	Voting Share, %
Ilija Batljan (privat och genom bolag)	109 053 868	1 137 606			13.2	40.1
Dragfast & Marjan Dragicevic	23 989 867	70 675 628			11.4	11.4
AB Arvid Svensson	26 000 000	34 296 667			7.2	10.8
Sven-Olof Johansson (genom bolag)	22 315 456	25 405 525			5.7	9.1
Erik Paulsson (genom bolag)	13 919 159	14 605 317			3.4	5.6
Michael Cocozza		45 326 742			5.5	1.7
Stiftelsen för Strategisk Forskning		42 651 810			5.1	1.6
Lennart Schuss (privat och genom bolag)	2 634 957	15 624 060			2.2	1.5
HighHill Intressenter AB		40 701 897			4.9	1.5
Oscar Lekander	3 174 785	1 536 200	275 500		0.6	1.2
Krister Karlsson	3 174 785	53 172			0.4	1.2
Postens pensionsstiftelse		19 004 310			2.3	0.7
Joakim Bill	1 904 871				0.2	0.7
Istappen Invest	1 587 393	906 794			0.3	0.6
Mille Dragicevic		11 572 058	660 627		1.5	0.4
Övriga	2 222 350	222 573 754	75 562 103	30 713	36.1	11.9
Total	**209 977 491**	**546 071 540**	**76 498 230**	**30 713**	**100**	**100**

Source: SBB, 2019c

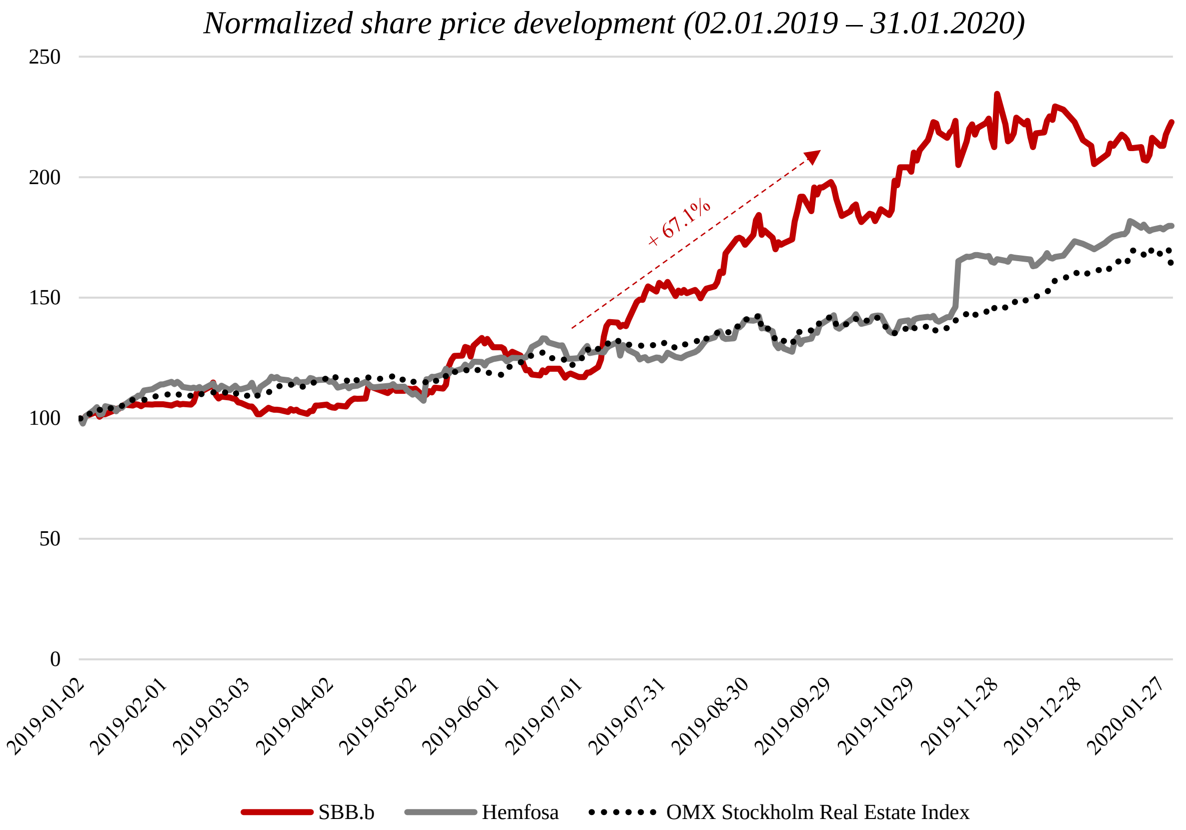
10.8 Hemfosa – ownership structure

As of 30.09.2019

	Number of shares		Percentage of	
Owners	Ordinary shares	Preference shares	Share capital, %	Voting rights, %
Swedbank Robur Funds	11,453,959	–	6.3	6.7
Länsförsäkringar Funds	11,293,013	–	6.3	6.6
SEB Funds	7,851,667	–	4.4	4.6
Norges Bank	6,194,358	–	3.4	3.6
Vanguard	5,139,044	508,938	3.1	3.0
Columbia Threadneedle	4,897,703	–	2.7	2.9
BlackRock	4,567,675	–	2.5	2.7
XACT Funds	3,333,855	–	1.8	2.0
ICA-handlarnas Förbund	2,900,000	–	1.6	1.7
Jens Engwall	2,500,000	–	1.4	1.5
Other	109,356,975	10,491,061	66.5	64.7
Total	**169,488,249**	**10,999,999**	**100.0**	**100.0**

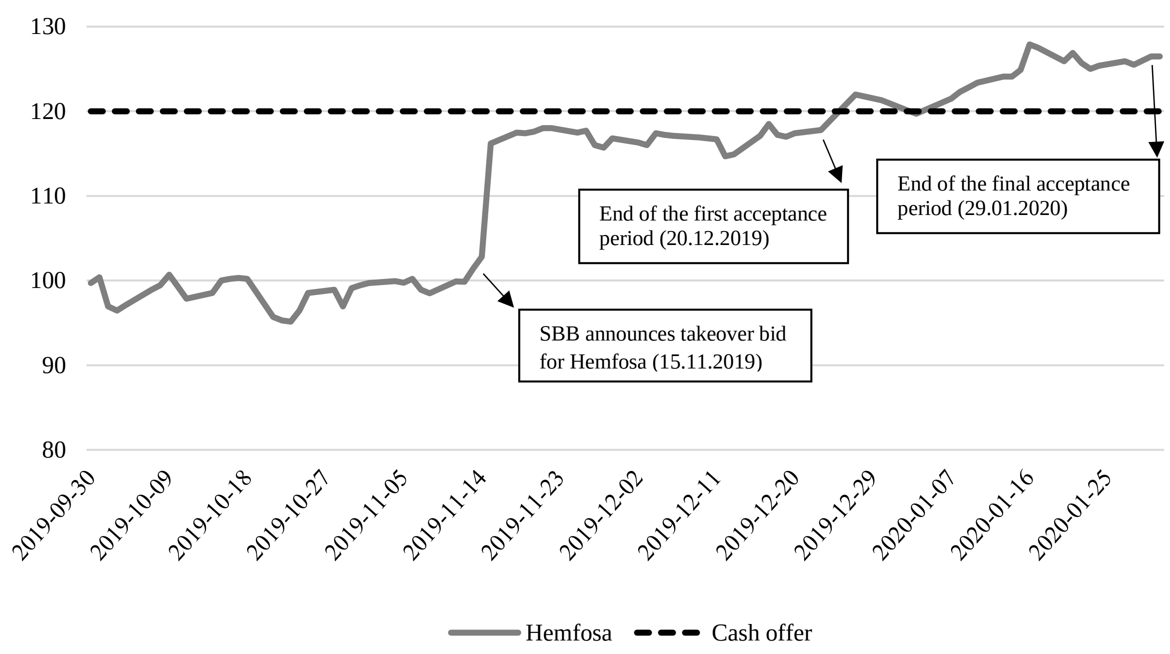
Source: Hemfosa, 2019b

10.9 Share price developments



Source: Eikon, 2020

Hemfosa common share price development and SBB cash offer (30.09.2019 – 31.01.2020)



Source: Eikon, 2020

10.10 SBB takeover offer for Hemfosa

The Offer

At announcement, the Offer values each Hemfosa common share at SEK 126.15 and each Hemfosa preference share at SEK 194.63 and the Total Offer Value is approximately SEK 23,521 million.[7] The Total Offer Value is comprised of the Total Common Offer Value of approximately SEK 21,380 million and the Total Preference Offer Value of approximately SEK 2,141 million.[8]

No commission will be charged in connection with the Offer.

Offer for common shares in Hemfosa

The total Offer consideration for Hemfosa common shares consists of a combination of cash and SBB Class B common shares. Subject to the potential adjustment of each individual Hemfosa shareholder's consideration due to elections made under the Common Mix & Match Facility as described below, SBB is offering each Hemfosa shareholder (the Common Base Case Consideration)[9]:

- in respect of 55 percent of the number of Hemfosa common shares tendered by such shareholder, 5.5 SBB Class B common shares per Hemfosa common share;[10] and
- in respect of the remaining 45 percent of the number of Hemfosa common shares tendered by such shareholder, SEK 120.00 in cash per Hemfosa common share.

[7] The Total Offer value of approximately SEK 23,521 is based on (i) a closing price of SBB Class B common shares of SEK 23.85 per share on Nasdaq Stockholm on 14 November 2019 and a closing price of SBB Class D common shares of SEK 34.70 per share on Nasdaq Stockholm on 14 November 2019, and (ii) 169,488,249 number of outstanding Hemfosa common shares and 10,999,999 outstanding Hemfosa preference shares as of 15 November 2019.
[8] Based on 169,488,249 outstanding common shares and 10,999,999 outstanding preference shares in Hemfosa and a closing price of SBB Class B common shares of SEK 23.85 per share on Nasdaq Stockholm on 14 November 2019, the last trading day before the announcement of the Offer and a closing price of SBB Class D common shares of SEK 34.70 per share on Nasdaq Stockholm on 14 November 2019, the last trading day before the announcement of the Offer.
[9] Assuming no election is made under the Common Mix & Match Facility (see below). In the event that Hemfosa should pay any dividend or make any other value transfer prior to the settlement of the Offer, the consideration in the Offer will be reduced correspondingly.
[10] Based on the closing price of SBB Class B common shares of SEK 23.85 per share on Nasdaq Stockholm on 14 November 2019, 5.5 SBB Class B common shares equates to a value per Hemfosa common share of SEK 131.18.

The cash paid to Hemfosa common shareholders is below referred to as the "**Common Cash Consideration**" and the shares paid to Hemfosa common shareholders is referred to as the "**Common Share Consideration**".

As an alternative, each Hemfosa common shareholder that is registered as owner of 50 or less Hemfosa common shares, is entitled to elect to receive an all cash consideration of SEK 120.00 per common share for all, but not only for some, of such shareholder's Hemfosa common shares.

The Common Base Case Consideration in the Offer represents premiums of:

- 22.7 percent compared to the closing price of SEK 102.80 of the Hemfosa common shares on Nasdaq Stockholm on 14 November 2019, the last trading day before the announcement of the Offer;
- 27.2 percent compared to the volume-weighted average share price of the Hemfosa common shares on Nasdaq Stockholm during the last month up to and including 14 November 2019; and
- 50.6 percent compared to Hemfosa's EPRA NAV[11] per common share of SEK 83.75 as of 30 September 2019.

Mix & Match Facility for Hemfosa common shareholders

SBB offers Hemfosa common shareholders a Mix & Match Facility (the "**Common Mix & Match Facility**"), through which each Hemfosa common shareholder is, subject to the restrictions set out below, given the possibility to elect, either:

(i) to receive as much Common Cash Consideration as possible for tendered Hemfosa common shares (in addition to the default cash entitlement of SEK 120.00 per Hemfosa common share in respect of 45 percent of the number of Hemfosa common shares tendered by such shareholder), and thus as little Common Share Consideration as possible,[12] or

(ii) to receive as much Common Share Consideration as possible for tendered Hemfosa common shares (in addition to the default share entitlement of 5.5 SBB Class B common shares per Hemfosa common share in respect of 55 percent of the number of Hemfosa common shares tendered by such shareholder), and thus as little Common Cash Consideration as possible.[13]

In aggregate, up to a total of 512,701,953 SBB Class B common shares will be issued, and up to a total of SEK 9,152 million will be paid in cash as consideration for Hemfosa common shares.[14] This proportion will not be varied as a result of elections made under the Common Mix & Match Facility. In order for individual shareholders in Hemfosa to receive a higher proportion of a certain requested consideration alternative under the Common Mix & Match Facility, other shareholders must have made the reverse elections to a corresponding extent. If no election is made under the Common Mix & Match Facility, the Hemfosa common shares tendered will be tendered for the Common Base Case Consideration.

[11] Net Asset Value Per Ordinary Share.

[12] A cash consideration of SEK 120.00 per Hemfosa common share would represent a premium of 16.7 percent compared to the closing price of SEK 102.80 of the Hemfosa common shares on Nasdaq Stockholm on 14 November 2019, the last trading day before the announcement of the Offer, and 21.0 percent compared to the volume-weighted average share price of the Hemfosa common shares on Nasdaq Stockholm during the last month up to and including 14 November 2019.

[13] A share consideration of 5.5 SBB Class B common shares per Hemfosa common share would represent a premium of 27.6 percent compared to the closing price of SEK 102.80 of the Hemfosa common shares on Nasdaq Stockholm on 14 November 2019, the last trading day before the announcement of the Offer, and 32.3 percent compared to the volume-weighted average share price of the Hemfosa common shares on Nasdaq Stockholm during the last month up to and including 14 November 2019, based on the closing price of SEK 23.85 of the SBB Class B common shares on Nasdaq Stockholm on 14 November 2019.

[14] Based on full acceptance in the Offer, and assuming all Hemfosa shareholders holding 50 or less Hemfosa common shares elect to receive 100 percent of the consideration in cash. At a lower acceptance level, the number of shares to be issued, and the total amount of cash to be paid, will be reduced proportionately to maintain the aggregate proportions in the Offer of new SBB shares issued and cash paid.

Hemfosa shareholders should be aware that the value of the Common Share Consideration will change over time in line with the SBB Class B common share price, which entails that elections made under the Common Mix & Match Facility may result in a higher or lower value per Hemfosa common share than the value of the Common Base Case Consideration.

If tenders made by Hemfosa common shareholders under the Common Mix & Match Facility are not fully matched, they will be scaled down on a pro rata basis in relation to the number of shares tendered by the respective shareholder.

Offer for preference shares in Hemfosa

The total Offer consideration for Hemfosa preference shares consists of a combination of cash and SBB Class D common shares. Subject to the potential adjustment of each individual Hemfosa shareholder's consideration due to elections made under the Preference Mix & Match Facility as described below, SBB is offering each Hemfosa preference shareholder (the Preference Base Case Consideration)[15]:

- in respect of 55 percent of the number of Hemfosa preference shares tendered by such shareholder, 5.6 SBB Class D common shares per Hemfosa preference share;[16] and

- in respect of the remaining 45 percent of the number of Hemfosa preference shares tendered by such shareholder, SEK 195.00 in cash per Hemfosa preference share.

The cash paid to Hemfosa preference shareholders is below referred to as the "**Preference Cash Consideration**" and the shares paid to Hemfosa preference shareholders is referred to as the "**Preference Share Consideration**".

As an alternative, each Hemfosa preference shareholder that is registered as owner of 25 or less Hemfosa preference shares, is entitled to elect to receive an all cash consideration of SEK 195.00 per preference share for all, but not only for some, of such shareholder's Hemfosa preference shares.

The Preference Base Case Consideration in the Offer represents premiums of:

- 1.1 percent compared to the closing price of SEK 192.50 of the Hemfosa preference shares on Nasdaq Stockholm on 14 November 2019, the last trading day before the announcement of the Offer; and
- 1.7 percent compared to the volume-weighted average share price of the Hemfosa preference shares on Nasdaq Stockholm during the last month up to and including 14 November 2019.

Mix & Match Facility for Hemfosa preference shareholders

SBB offers Hemfosa shareholders a Mix & Match Facility (the "**Preference Mix & Match Facility**"), through which each Hemfosa preference shareholder is, subject to the restrictions set out below, given the possibility to elect, either:

(i) to receive as much Preference Cash Consideration as possible for tendered Hemfosa preference shares (in addition to the default cash entitlement of SEK 195.00 per Hemfosa preference share in respect of 45 percent of the number of Hemfosa preference shares

[15] Assuming no election is made under the Preference Mix & Match Facility (see below). In the event that Hemfosa should pay any dividend or make any other value transfer prior to the settlement of the Offer, the consideration in the Offer will be reduced correspondingly.
[16] Based on the closing price of SBB Class D common shares of SEK 34.70 per share on Nasdaq Stockholm on 14 November 2019, 5.6 SBB Class D common shares equates to a value per Hemfosa common share of SEK 194.32.

tendered by such shareholder), and thus as little Preference Share Consideration as possible,[17] or

(ii) to receive as much Preference Share Consideration as possible for tendered Hemfosa preference shares (in addition to the default share entitlement of 5.6 SBB Class D common shares per Hemfosa preference share in respect of 55 percent of the number of Hemfosa preference shares tendered by such shareholder), and thus as little Preference Cash Consideration as possible.[18]

In aggregate, up to a total of 33,879,996 SBB Class D common shares will be issued, and up to a total of SEK 965 million will be paid in cash as consideration for Hemfosa preference shares.[19] This proportion will not be varied as a result of elections made under the Preference Mix & Match Facility. In order for individual shareholders in Hemfosa to receive a higher proportion of a certain requested consideration alternative under the Preference Mix & Match Facility, other shareholders must have made the reverse elections to a corresponding extent. If no election is made under the Preference Mix & Match Facility, the Hemfosa preference shares tendered will be tendered for the Preference Base Case Consideration.

Hemfosa shareholders should be aware that the value of the Preference Share Consideration will change over time in line with the SBB Class D common share price, which entails that elections made under the Preference Mix & Match Facility may result in a higher or lower value per Hemfosa preference share than the value of the Preference Base Case Consideration.

If tenders made by Hemfosa preference shareholders under the Preference Mix & Match Facility are not fully matched, they will be scaled down on a pro rata basis in relation to the number of shares tendered by the respective shareholder.

Fractions

No fractions of SBB Class B common shares or SBB Class D common shares will be delivered to shareholders in Hemfosa accepting the Offer. If a shareholder in Hemfosa tenders a number of Hemfosa shares in the Offer and the share consideration to be delivered for these shares does not amount to an even number of full new SBB Class B common shares and/or SBB Class D common shares, consideration for excess fractions of shares will be paid in cash.

Rights under Hemfosa's incentive programs

The Offer does not include warrants, or other rights, issued by Hemfosa to employees under Hemfosa's incentive programs. SBB will procure for a fair treatment in connection with the Offer for the participants in such program in accordance with the Takeover Rules issued by Nasdaq Stockholm.

Recommendation from the board of directors of Hemfosa

The board of directors of Hemfosa unanimously recommend the shareholders of Hemfosa to accept the Offer. The board of directors of Hemfosa has received a fairness opinion from Handelsbanken Capital

[17] A cash consideration of SEK 195.00 per Hemfosa preference share would represent a premium of 1.3 percent compared to the closing price of SEK 192.50 of the Hemfosa preference shares on Nasdaq Stockholm on 14 November 2019, the last trading day before the announcement of the Offer, and 1.9 percent compared to the volume-weighted average share price of the Hemfosa preference shares on Nasdaq Stockholm during the last month up to and including 14 November 2019.

[18] A share consideration of 5.6 SBB Class D common shares per Hemfosa preference share would represent a premium of 0.9 percent compared to the closing price of SEK 192.50 of the Hemfosa preference shares on Nasdaq Stockholm on 14 November 2019, the last trading day before the announcement of the Offer, and 1.6 percent compared to the volume-weighted average share price of the Hemfosa preference shares on Nasdaq Stockholm during the last month up to and including 14 November 2019, based on the closing price of SEK 34.70 of the SBB Class D common shares on Nasdaq Stockholm on 14 November 2019.

[19] Based on full acceptance in the Offer, and assuming all Hemfosa shareholders holding 25 or less Hemfosa preference shares elect to receive 100 percent of the consideration in cash. At a lower acceptance level, the number of shares to be issued, and the total amount of cash to be paid, will be reduced proportionately to maintain the aggregate proportions in the Offer of new SBB shares issued and cash paid.

Markets concluding that, subject to the qualifications and assumptions set out therein, the Offer from a financial point of view, is fair to the common and preference shareholders of Hemfosa.

SBB's shareholding in Hemfosa

Neither SBB nor any of its affiliated parties currently holds or controls any shares or any other financial instruments in Hemfosa.

Neither SBB nor any of its affiliated parties has acquired or agreed to acquire any shares in Hemfosa, or any other financial instruments that give a financial exposure equivalent to a shareholding in Hemfosa, during the six month-period preceding the announcement of the Offer.

SBB may acquire, or enter into arrangements to acquire, shares in Hemfosa outside the Offer and any purchases made or arranged will be disclosed in accordance with applicable rules.

Statement by shareholders

Jens Engwall, holding approximately 1.4 percent of the shares and 1.5 percent of the voting rights in Hemfosa, has stated that he is positive to the Offer, but has not entered into any undertaking, or other arrangement, to accept the Offer.

Conditions for the Offer

Completion of the Offer is conditional upon:

(1) the Offer being accepted to such an extent that SBB becomes the owner of shares representing more than 90 percent of the outstanding shares in Hemfosa on a fully diluted basis;

(2) no other party announcing an offer to acquire shares in Hemfosa on terms that are more favorable to the shareholders of Hemfosa than the Offer;

(3) with respect to the Offer and the acquisition of Hemfosa, receipt of all necessary regulatory, governmental or similar clearances, approvals and decisions, including from competition authorities, in each case on terms which, in SBB's opinion, are acceptable;

(4) neither the Offer nor the acquisition of Hemfosa being rendered wholly or partially impossible or significantly impeded as a result of legislation or other regulation, any decision of a court or public authority, or any similar circumstance;

(5) no circumstances having occurred which could have a material adverse effect or could reasonably be expected to have a material adverse effect on Hemfosa's financial position or operation, including Hemfosa's sales, results, liquidity, equity ratio, equity or assets;

(6) no information made public by Hemfosa or disclosed by Hemfosa to SBB being inaccurate, incomplete or misleading, and Hemfosa having made public all information which should have been made public; and

(7) Hemfosa not taking any action that is likely to impair the prerequisites for making or completing the Offer.

SBB reserves the right to withdraw the Offer in the event that it is clear that any of the above conditions is not satisfied or cannot be satisfied. However, with regard to conditions (2)-(7), the Offer may only be withdrawn where the non-satisfaction of such condition is of material importance to SBB's acquisition of Hemfosa.

Financing

The Offer is not subject to any financing condition. The Offer, in regard to the total cash consideration payable under the Offer, is fully financed by SBB's own balance sheet and a new bridge facility arranged by J.P. Morgan Securities plc ("**J.P. Morgan**") as sole mandated lead arranger. The conditions to drawdown are usual and customary for a facility of this type.

As part of the consideration in the Offer, SBB may issue up to a total of 512,701,953 new SBB Class B common shares and up to a total of 33,879,996 new SBB Class D common shares to Hemfosa shareholders for the payment of the total share consideration under the Offer, which would give Hemfosa shareholders a 37.4 percent ownership of capital and 16.3 percent of the votes in the combined business on a post SBB Rights Issue basis.[20] The resolution to issue such shares will be resolved by SBB's board of directors based on an authorisation granted by the annual general meeting held on 29 April 2019 and is, as such, not subject to any approval by the general meeting.

Due diligence

SBB has, in connection with the preparations for the Offer, conducted a limited due diligence review of confirmatory nature of Hemfosa. Hemfosa has advised SBB that SBB has not received any inside information in connection with the due diligence review.

Indicative timetable

The acceptance period for the Offer is expected to commence around 19 November 2019 and end around 20 December 2019. An offer document regarding the Offer is expected to be made public shortly before the commencement of the acceptance period. Assuming that the Offer is declared unconditional no later than around 23 December 2019, settlement is expected to begin around 3 January 2020.

The transaction requires the approval of the Swedish merger control authority. SBB will file the transaction shortly after its announcement and relevant clearances are expected to be obtained prior to the end of the acceptance period.

SBB reserves the right to extend the acceptance period for the Offer and to postpone the settlement date.

Compulsory acquisition and delisting

In the event that SBB, whether in connection with the Offer or otherwise, becomes the owner of shares representing more than 90 percent of the outstanding shares in Hemfosa, SBB intends to commence a compulsory acquisition procedure under the Swedish Companies Act to acquire all remaining shares in Hemfosa. In connection therewith, SBB intends to promote a de-listing of the Hemfosa shares from Nasdaq Stockholm.

Source: SBB, 2019e

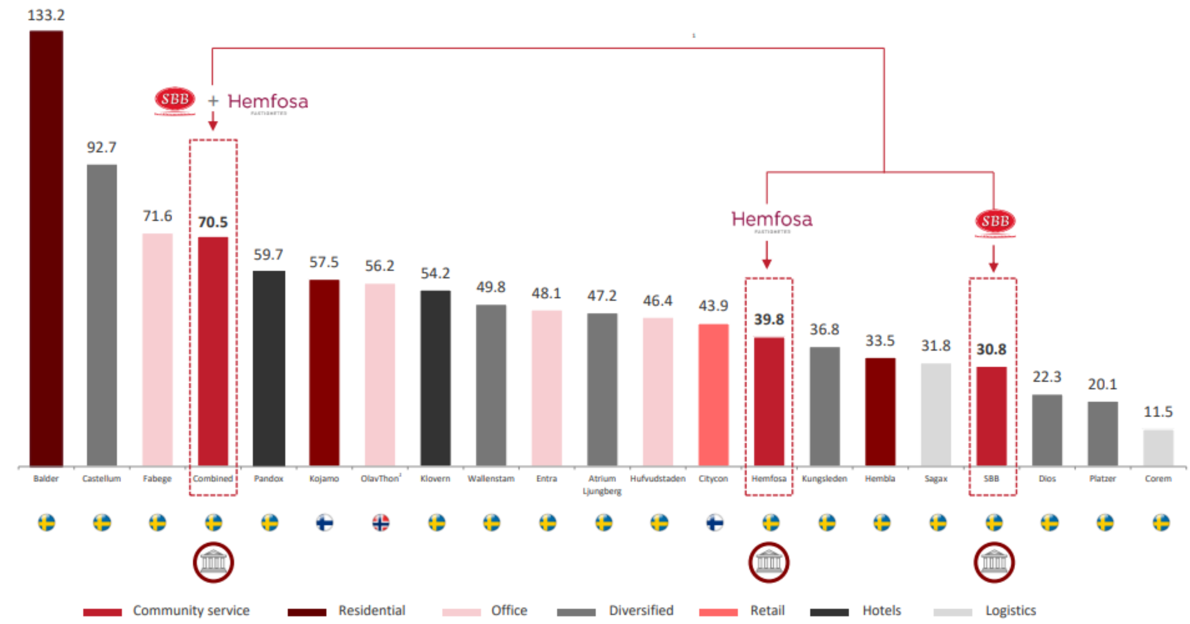
10.11 SBB offer presentation - The combined company

A COMBINATION OF SBB AND HEMFOSA HAS A COMPELLING STRATEGIC RATIONALE

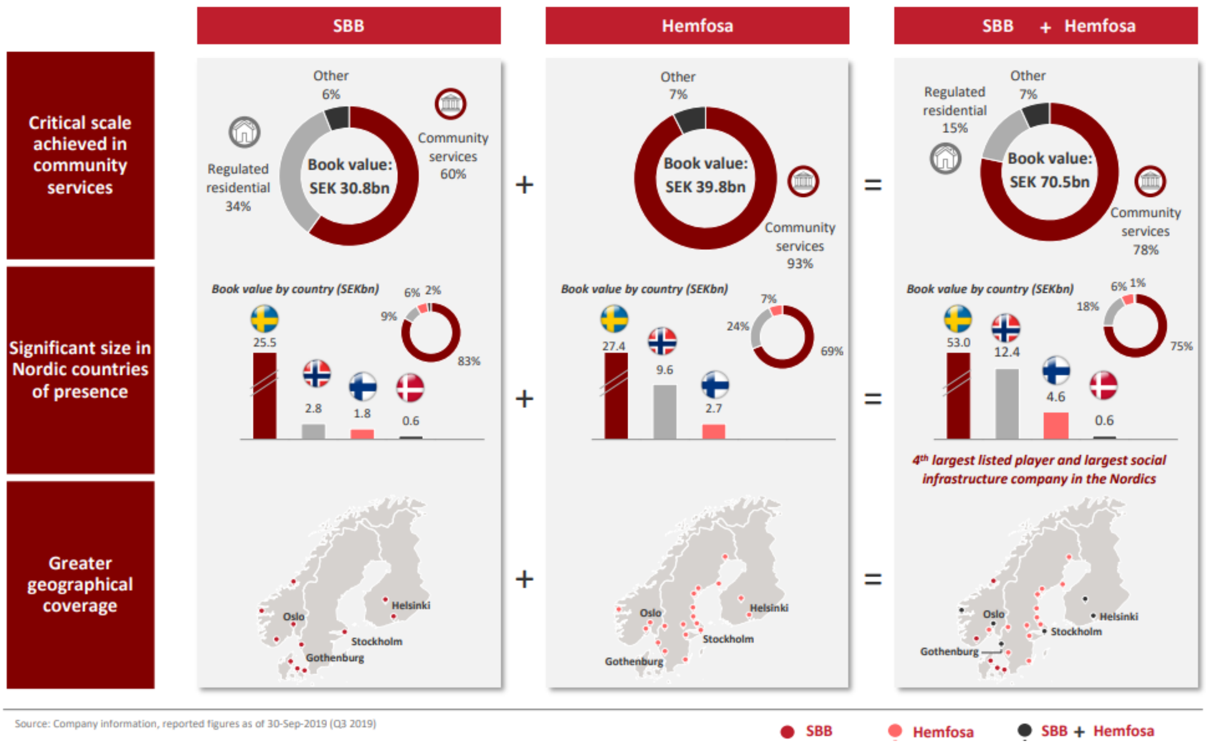
1. Transformational transaction creating the 4th largest listed player and the social infrastructure property champion in the Nordics
2. Significantly enhanced exposure to the highly attractive and very low risk social infrastructure real estate sector
3. Strengthened balance sheet and financials, improving SBB's KPIs and accelerating delivery of financial and operational targets
4. Opportunity to unlock significant synergies and value creation, optimising best practices and benefiting from SBB's active asset management
5. Aligned sustainability frameworks, accelerating environmental initiatives towards a more sustainable world

COMBINED PORTFOLIO: THE SOCIAL INFRASTRUCTURE PROPERTY CHAMPION AND 4TH LARGEST LISTED PLAYER IN THE NORDICS

Top 20 listed Nordic players by GAV (SEK bn)



COMBINED PORTFOLIO GAINS SIGNIFICANTLY INCREASED SCALE AND GREATER GEOGRAPHICAL COVERAGE

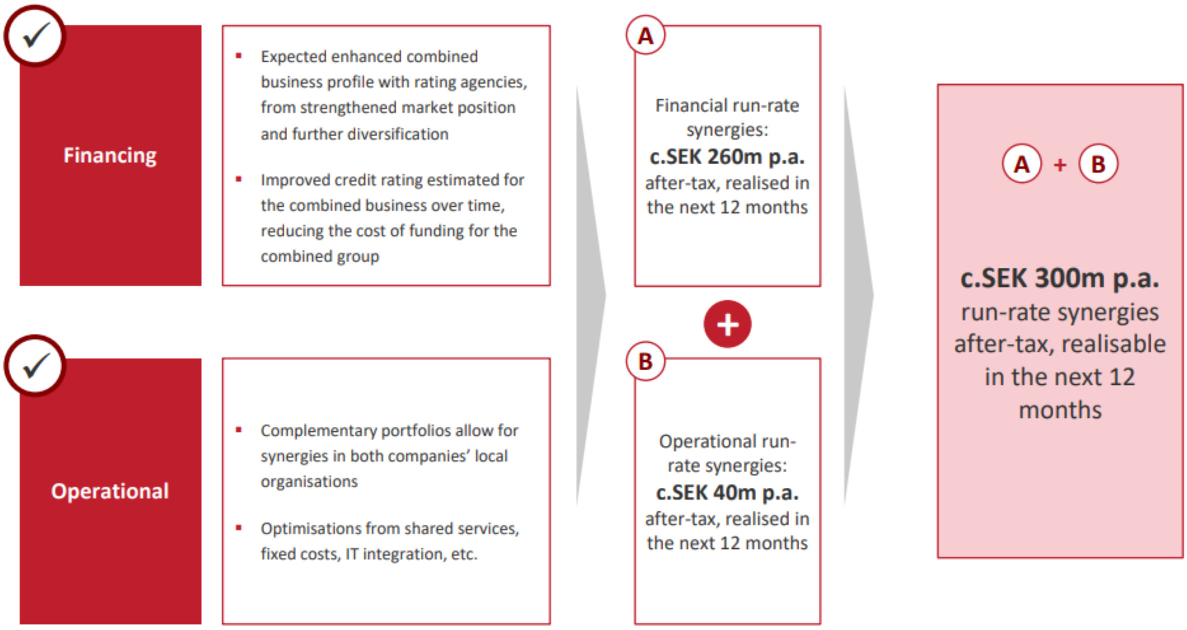


STRONG PROFIT WITH FINANCIAL UPSIDE

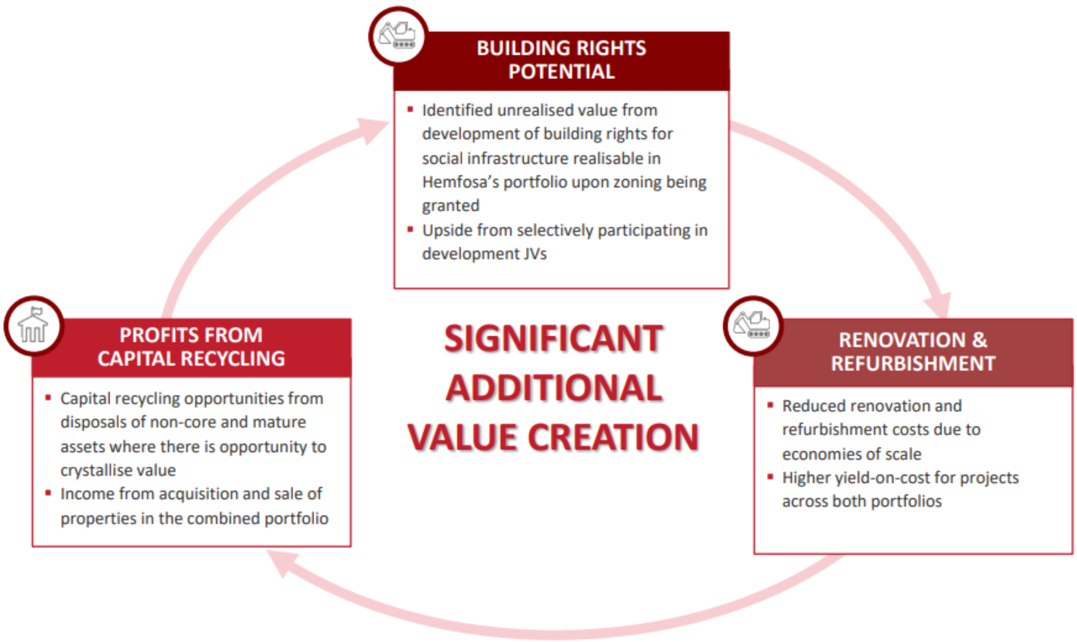
Key portfolio metrics	SBB	Hemfosa	SBB + Hemfosa
Portfolio book value (SEKbn)	30.8	39.8	**70.5**
Lettable area (m sqm)	1.8	2.2	**4.0**
Net initial yield[1]	4.7%	5.4%	**5.1%**
Economic occupancy[3]	95.3%	94.2%	**94.7%**
Lease maturity (years)[3]	7.0[2] (effectively perpetual)	6.5 (effectively perpetual)	**6.7 (effectively perpetual)**
Portfolio book value / sqm (SEK)[4]	16,397	18,261	**17,419**
Passing rent / sqm (SEK)	1,116	1,329	**1,233**
Net LTV (as % of total assets)[5]	37.1%[8]	56.1%	**< 50%[5]** 2020E
ICR	2.4x[6]	3.6x[7]	**> 3.0x** 2020E
Net profit for the period – 9M 2019 (SEKm)	1,337	1,497	**2,834**

Source: Company information, reported figures as of 30-Sep-2019 (3Q 2019); the aggregation should not be viewed as a pro-forma but as an arithmetic sum of SBB and Hemfosa metrics; SBB may publish pro forma reports which will set out any relevant assumptions and adjustments to such calculations applicable under relevant accounting rules. Notes: [1] Calculated as passing NOI divided by GAV. For SBB and in a combined basis, GAV excludes building rights value of SEK 1,343m at SBB level; [2] Refers to community service properties segment only; [3] Weighted average based on lettable area; [4] Calculated as GAV (excluding building rights value of SEK 1,343m at SBB and combination level) divided by lettable area; [5] Net LTV, taken as a % of total assets, excluding lease liability and hybrids treated at 100% equity; [6] Profit from property management (last 12 months) after reversal of financial expenses in relation to financial expenses excluding costs for early redemption of loans and land lease fees; [7] Profit from property management, including reversal of financial income and expenses, as well as depreciation/amortisation and share in profit in JVs as a % of financial income and expenses; [8] Adjusted pro-forma for SEK 400m issue of B shares on 23-Oct-2019

SUBSTANTIAL SYNERGIES DRIVING TOTAL SHAREHOLDER RETURN



SIGNIFICANT ADDITIONAL VALUE CREATION OPPORTUNITIES FOR ALL SHAREHOLDERS



Source: SBB, 2019l

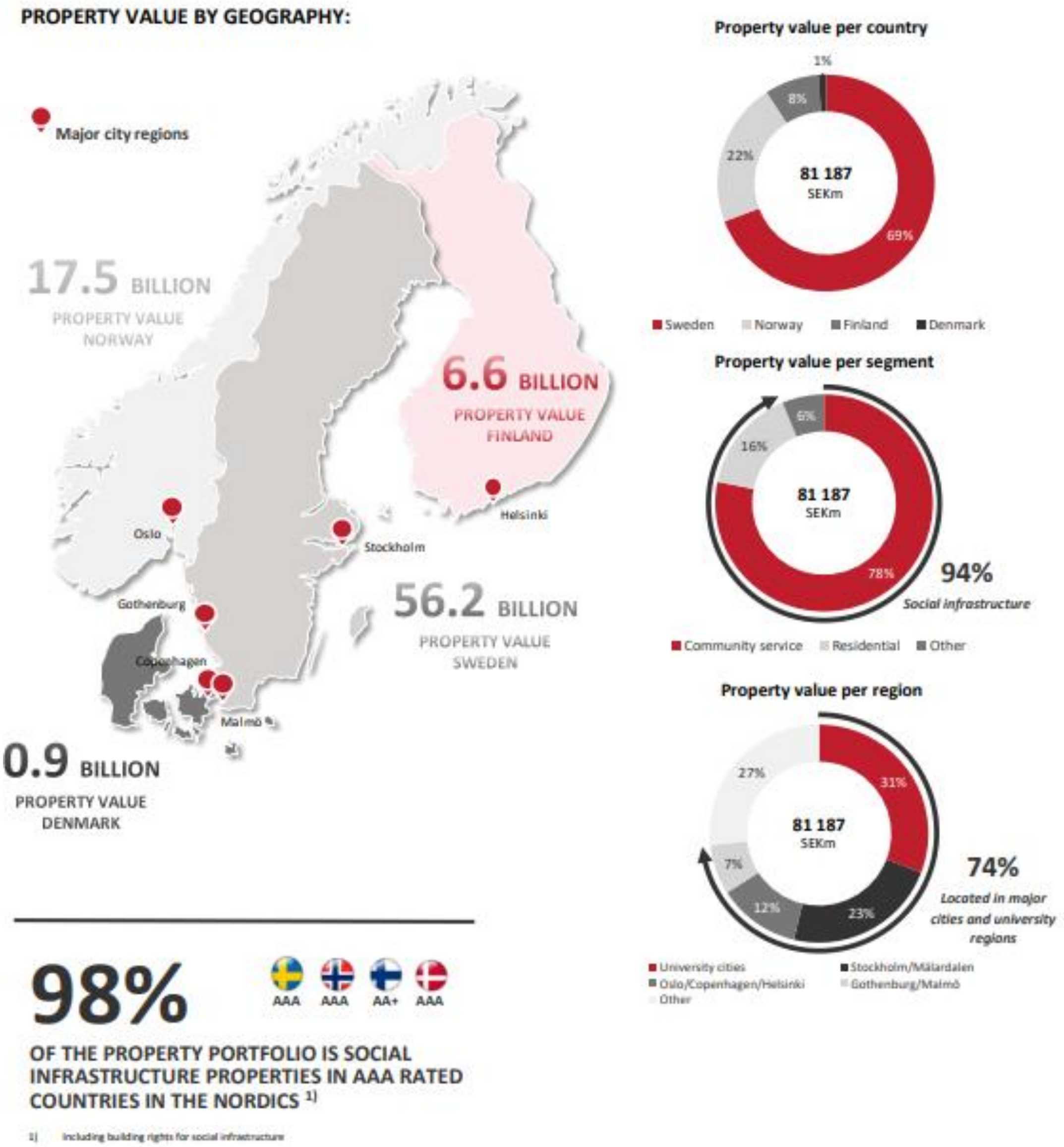
10.12 Transaction process timeline

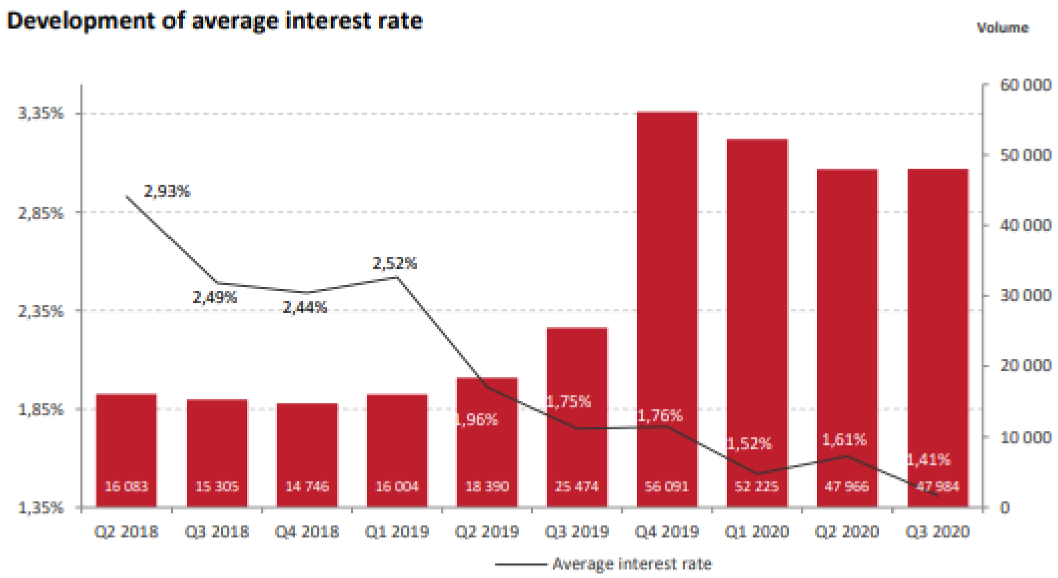
15-11-2019	SBB announces takeover offer
19-11-2019	Start of acceptance period
26-11-2019	SBB receives competition clearence
04-12-2019	Länsförsäkringar and ICA publicly supports the offer
18-12-2019	SBB divests holdings in Amasten Fastighets AB (Publ)
19-12-2019	Swedbank publicly supports the offer
20-12-2019	End of first acceptance period
23-12-2019	SBB controls 87.8% of the capital and 88.1% of the votes, and SBB declares the offer unconditional and extends the acceptance period to January 15th
10-01-2020	SBB controls 91.2% of the capital and 91.6% of the votes
15-01-2020	End of second acceptance period
17-01-2020	SBB controls 92.6% of the capital and 92.9% of the votes, and SBB declares the offer unconditional and extends the acceptance period to January 29th
29-01-2020	End of the last acceptance period
31-01-2020	Hemfosa is delisted from Nasdaq Stockholm, and SBB controls 93.5% of the capital and 93.8% of the votes

Source: SBB press releases

10.13 The combined entity

As of 30.09.2020





Source: SBB, 2020d

10.14 Authors' valuation of Hemfosa Fastigheter AB

10.14.1 Hemfosa standalone valuation (base case)

Present value as of Sep 30, 2019 *(as proxy for Nov 14, 2019)*

Standalone value - Hemfosa Fastigheter AB (base case)

Nominal discount rate contracted NOI (1)	5.20%
Nominal discount rate terminal value NOI (2)	7.00%
Terminal growth (3)	2.00%

	(Oct-Dec)	(Analyst forecast) (5)		(Authors estimate)			
(in SEK millions)	**Q4 2019E (4)**	**2020E**	**2021E**	**2022E**	**2023E**	**2024E**	**2025E**
Years to discount	0.25	1.25	2.25	3.25	4.25	5.25	6.25
Property portfolio value (6)	**39,913**	**40,438**	**41,088**	**45,917**	**46,835**	**48,727**	**49,702**
Value from yield compression	n/a	0	0	883	0	955	0
Yield compression	*n/a*	*0.0%*	*0.0%*	*-0.1%*	*0.0%*	*-0.1%*	*0.0%*
Rental income	728	3,024	3,145	3,208	3,272	3,337	3,404
nominal growth (%)	*n/a*	*5.9%*	*4.0%*	*2.0%*	*2.0%*	*2.0%*	*2.0%*
Property expenses	-211	-834	-848	-866	-883	-901	-919
Net operating income	**517**	**2,190**	**2,297**	**2,342**	**2,389**	**2,436**	**2,485**
NOI margin	*71.0%*	*72.4%*	*73.0%*	*73.0%*	*73.0%*	*73.0%*	*73.0%*
Central administration costs	-32	-128	-130	-133	-135	-138	-141
% of income	*-4.4%*	*-4.2%*	*-4.1%*	*-4.1%*	*-4.1%*	*-4.1%*	*-4.1%*
Other operating income/costs	7	16	16	16	17	17	17
% of income	*1.0%*	*0.5%*	*0.5%*	*0.5%*	*0.5%*	*0.5%*	*0.5%*
Adjusted operating income	**492**	**2,078**	**2,183**	**2,225**	**2,270**	**2,315**	**2,362**
Discount rate contracted NOI (7)	*5.2%*	*5.2%*	*5.2%*	*5.1%*	*5.1%*	*5.0%*	*5.0%*
Discount factor	0.9874	0.9386	0.8922	0.8507	0.8094	0.7740	0.7372
Present value (NOI)	**486**	**1,950**	**1,948**	**1,893**	**1,837**	**1,792**	**1,741**
Terminal value (8)							**48,179**
Discount rate terminal value NOI							*7.0%*
Discount factor							0.6552
Present value terminal value NOI							**31,565**

Enterprise value (Hemfosa)	**43,213**
Cash balance	616
Interest bearing debt (30.09.2019)	-23,774
Market capitalization preference shares (9)	-2,140
Equity value common shares	**17,915**
Common shares outstanding (mn)	*169.488*
Value per common share	**105.70**
Prevailing share value (14.11.2019)	*102.80*
Prevailing EPRA NAV per share (30.09.2019)	*83.75*
Prevailing CE rolling 12 (mn) (30.09.2019)	*1,374*

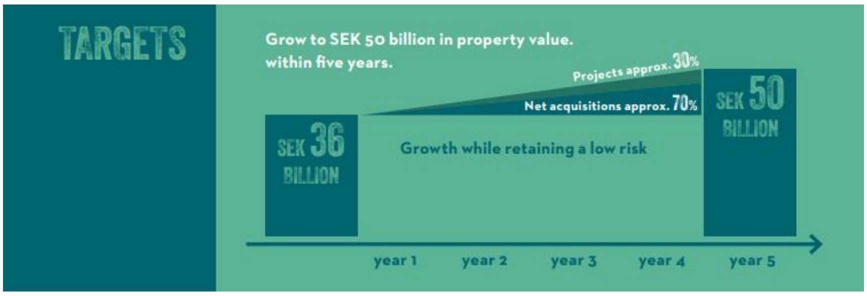
Authors' standalone vaulation		
Share premium	**P / EPRA NAV premium**	**P / CE**
2.8%	26.2%	13.0x

SBB takeover offer (10)		
Share premium	**P / EPRA NAV premium**	**P / CE**
22.7%	50.6%	15.6x

(22,7% on 14 November 2019)

(1) Hemfosa real yield requirement (2019) + 1% inflation – 1% discount due to contracted cash flows with an average duration of 6.5 years (i.e. locked-in cash flows). Assumption based on interview (23.10.2020, Lindmark).
(2) Authors' discount rate FY2025E (5%) + 2% long-term inflation (Swedish Riksbank long-term inflation target)
(3) Authors' estimate based on long-term inflation target
(4) Estimated as a residual between Carnegie full-year estimate 2019 and reported YTD figures Q3 2019 (Hemfosa, 2019b)
(5) Carnegie analyst report forecast (Carnegie, 2019)
(6) For 2022E–2025E calculated as: Net operating income / Discount rate contracted NOI (yield)
(7) Authors' assumption based on market's belief of further yield compression (review *Yields* in Appendix 10.4)
(8) Calculated based on Gordon Growth formula
(9) As of 30.09.2019. Prevailing share price of SEK 194.5 * number of preference shares outstanding (11mn)
(10) SBB offer value corresponds to November 15th, 2019. Share premium on November 14th, 2019 = 22.7%

10.14.2 Hemfosa standalone valuation (growth case)



Source: Hemfosa, 2018

Present value as of Sep 30, 2019 *(as proxy for Nov 14, 2019)*

Standalone value - Hemfosa Fastigheter AB (growth case)

Nominal discount rate contracted NOI (1)	5.20%
Nominal discount rate terminal value NOI (2)	7.00%
Terminal growth (3)	2.00%

(in SEK millions)	(Oct-Dec) **Q4 2019E** (4)	(Analysts) (5) **2020E**	(Authors estimate) **2021E**	**2022E**	**2023E**	**2024E**	**2025E**
Years to discount	0.25	1.25	2.25	3.25	4.25	5.25	6.25
Property portfolio value (6)	**39,913**	**40,438**	**44,575**	**47,721**	**50,107**	**52,132**	**53,174**
Value from yield compression	n/a	0	0	918	0	1,022	0
Yield compression	*n/a*	*0.0%*	*0.0%*	*-0.1%*	*0.0%*	*-0.1%*	*0.0%*
Rental income	728	3,024	3,175	3,334	3,501	3,571	3,642
nominal growth (%)	*n/a*	*5.9%*	*5.0%*	*5.0%*	*5.0%*	*2.0%*	*2.0%*
Property expenses	-211	-834	-857	-900	-945	-964	-983
Net operating income	**517**	**2,190**	**2,318**	**2,434**	**2,555**	**2,607**	**2,659**
NOI margin	*71.0%*	*72.4%*	*73.0%*	*73.0%*	*73.0%*	*73.0%*	*73.0%*
Central administration costs	-32	-128	-134	-141	-148	-151	-154
% of income	*-4.4%*	*-4.2%*	*-4.2%*	*-4.2%*	*-4.2%*	*-4.2%*	*-4.2%*
Other operating income/costs	7	16	17	18	19	19	19
% of income	*1.0%*	*0.5%*	*0.5%*	*0.5%*	*0.5%*	*0.5%*	*0.5%*
Adjusted operating income	**492**	**2,078**	**2,200**	**2,310**	**2,426**	**2,474**	**2,524**
Discount rate contracted NOI (7)	*n/a*	*5.2%*	*5.2%*	*5.1%*	*5.1%*	*5.0%*	*5.0%*
Discount factor	0.9874	0.9386	0.8922	0.8507	0.8094	0.7740	0.7372
Present values (NOI)	**486**	**1,950**	**1,963**	**1,965**	**1,964**	**1,915**	**1,860**
Terminal value (8)							**51,486**
Discount rate terminal value NOI							*7.0%*
Discount factor							0.6552
Present value terminal value NOI							**33,732**

Enterprise value (Hemfosa)	**45,836**
Cash balance	616
Interest bearing debt (30.09.2019)	-23,774
Market capitalization preference shares (9)	-2,140
Equity value common shares	**20,539**
Common shares outstanding (mn)	*169.488*
Value per common share	**121.18**
Prevailing share value (14.11.2019)	*102.80*
Prevailing EPRA NAV per share (30.09.2019)	*83.75*
Prevailing CE rolling 12 (mn) (30.09.2019)	*1,374*

Authors' standalone vaulation

Share premium	**EPRA NAV / share**	**P / CE**
17.9%	44.7%	14.9x

SBB takeover offer (10)

Share premium	**EPRA NAV / share**	**P / CE**
22.7%	50.6%	15.6x

- NOTE! Due to lack of data, the authors' valuation is based on reported figures as of 30.09.2019, which implies a slight timing difference compared to the actual offer announcement date 15.11.2019. Therefore, multiples from the authors' valuation are derived from the prevailing share price on 14.11.2019 and the authors' valuation as of 30.09.2019.

10.14.3 Valuation of deal synergies

Present value as of Sep, 30 2019 *(as a proxy for Nov, 14 2019)*

Synergy valuation - Hemfosa transaction (a)

Average cost of debt (30.09.2019) (b)	2.16%
Terminal growth rate financial synergies (c)	-5.00%
Terminal growth rate operational synergies (d)	0.00%

(in SEK millions)	(Oct-Dec) YTG 2019 (e)	2020E	2021E	2022E	2023E	2024E	2025E	Terminal Value (g)
Years to discount	0.25	1.25	2.25	3.25	4.25	5.25	6.25	
Financial synergies	*0*	*260*	*260*	*260*	*260*	*260*	*260*	*3,450*
Financial synergies (a.t.)	0	204	206	206	206	206	206	2,739
Operational synergies	*0*	*40*	*40*	*40*	*40*	*40*	*40*	*769*
Operational synergies (a.t.)	0	31	32	32	32	32	32	611
Cost to achieve synergies (f)	*-30*	*0*	*0*	*0*	*0*	*0*	*0*	*0*
Cost to achieve synergies (a.t.)	-24	0	0	0	0	0	0	0
Tax rate (h)	*21.40%*	*21.40%*	*20.60%*	*20.60%*	*20.60%*	*20.60%*	*20.60%*	*20.60%*
Discount rate financial synergies	*2.16%*	*2.16%*	*2.16%*	*2.16%*	*2.16%*	*2.16%*	*2.16%*	
Discount factor financial synergies	0.9947	0.9736	0.9531	0.9329	0.9132	0.8939	0.8750	
Present value of financial synergies	**0**	**199**	**197**	**193**	**189**	**185**	**181**	
Present value of TV financial synergies							**2,397**	
Discount rate operational synergies	*5.2%*	*5.2%*	*5.2%*	*5.2%*	*5.2%*	*5.2%*	*5.2%*	
Discount factor operational synergies	0.9874	0.9386	0.8922	0.8481	0.8062	0.7663	0.7285	
Present value of operational synergies	**-23**	**30**	**28**	**27**	**26**	**24**	**23**	
Present value of TV operational synergies							**445**	

PV (Synergies 2020E - 2025E)	**1,277**
PV (Terminal value synergies)	**2,842**
Value of synergies	**4,118**
Common shares outstanding (mn)	169.488
Value per common share	**24.30**

(a) Input data of SEK 260mn in annual financial synergies and SEK 40mn annual operational synergies, based on offer document (SBB, 2019e) and interviews.
(b) Hemfosa average interest rate in the loan book as of 30.09.2019 (Hemfosa, 2019b)
(c) Authors' assumption
(d) Authors' assumption
(e) No realized synergies YTG 2019 (Oct-Dec). Authors' assumption based on transaction closing date year-end 2019
(f) Authors' assumption. 10% of total annual synergies.
(g) Calculated based on Gordon Growth formula
(h) Swedish tax rate

Authors' valuations including synergies

Base case valuation output per share (SEK)	
Hemfosa standalone value per common share	105.70
Value of synergies per common share	24.30
Total value	**130.00**
% of synergies to Hemfosa given the SBB offer of 126.15 SEK / share	*84.2%*
% of synergies to SBB given the SBB offer of 126.15 SEK / share	*15.8%*

Growth case valuation output per share (SEK)	
Hemfosa standalone value per common share	121.18
Value of synergies per common share	24.30
Total value	**145.48**
% of synergies to Hemfosa given the SBB offer of 126.15 SEK / share	*20.5%*
% of synergies to SBB given the SBB offer of 126.15 SEK / share	*79.5%*

10.14.4 Sensitivity analysis

Authors' base case valuation per share

Discount rate contracted NOI	Discount rate terminal value NOI				
	6.80%	**6.90%**	**7.00%**	**7.10%**	**7.20%**
5.60%	114.83	109.70	104.79	100.07	95.55
5.40%	115.28	110.16	105.24	100.53	96.00
5.20%	115.74	110.62	105.70	100.99	96.46
5.00%	116.21	111.08	106.17	101.45	96.93
4.80%	116.68	111.55	106.64	101.92	97.40

Authors' growth case valuation per share

Discount rate contracted NOI	Discount rate terminal value NOI				
	6.80%	**6.90%**	**7.00%**	**7.10%**	**7.20%**
5.60%	128.51	124.28	120.21	116.31	112.56
5.40%	128.99	124.76	120.69	116.79	113.04
5.20%	129.47	125.24	121.18	117.28	113.52
5.00%	129.96	125.73	121.67	117.77	114.01
4.80%	130.46	126.23	122.16	118.26	114.51

Authors' valuation of synergies per share

Terminal growth financial synergies		Discount rate financial synergies				
		1.96%	**2.06%**	**2.16%**	**2.26%**	**2.36%**
	0.00%	65.25	62.23	59.50	57.00	54.72
	-2.50%	33.79	33.11	32.46	31.83	31.23
	-5.00%	24.93	24.61	24.30	23.99	23.70
	-7.50%	20.76	20.56	20.36	20.17	19.99
	-10.00%	18.32	18.18	18.04	17.91	17.77

Terminal growth operational synergies		Discount rate operational synergies				
		5.00%	**5.10%**	**5.20%**	**5.30%**	**5.40%**
	0.00%	24.44	24.37	24.30	24.23	24.16
	-2.50%	23.52	23.48	23.44	23.41	23.37
	-5.00%	23.06	23.03	23.01	22.98	22.96
	-7.50%	22.78	22.76	22.75	22.73	22.71
	-10.00%	22.60	22.58	22.57	22.55	22.54

10.14.5 Valuation comparable companies

As of 30.09.2019

Company	**MCAP ("P")** (i)	**EPRA NAV** (ii)	**P / EPRA NAV**	**Cash earnings ("CE")** (iii)	**P / CE**
SBB	14.257	9.914	144%	0.500	28.51x
Fabege	53.653	45.595	118%	1.422	37.73x
Castellum	57.591	50.730	114%	3.103	18.56x
Kungsleden	19.525	19.300	101%	1.185	16.48x
Klövern	22.748	15.244	149%	1.326	17.16x
Balder	62.918	56.471	111%	3.172	19.84x
Wihlborgs	24.594	20.018	123%	1.691	14.54x
Wallenstam	32.978	28.210	117%	1.181	27.92x
Median			**117%**		**19.20x**
Average			**122%**		**22.59x**
Hemfosa	16.898	14.195	**119%**	1.374	**12.30x**

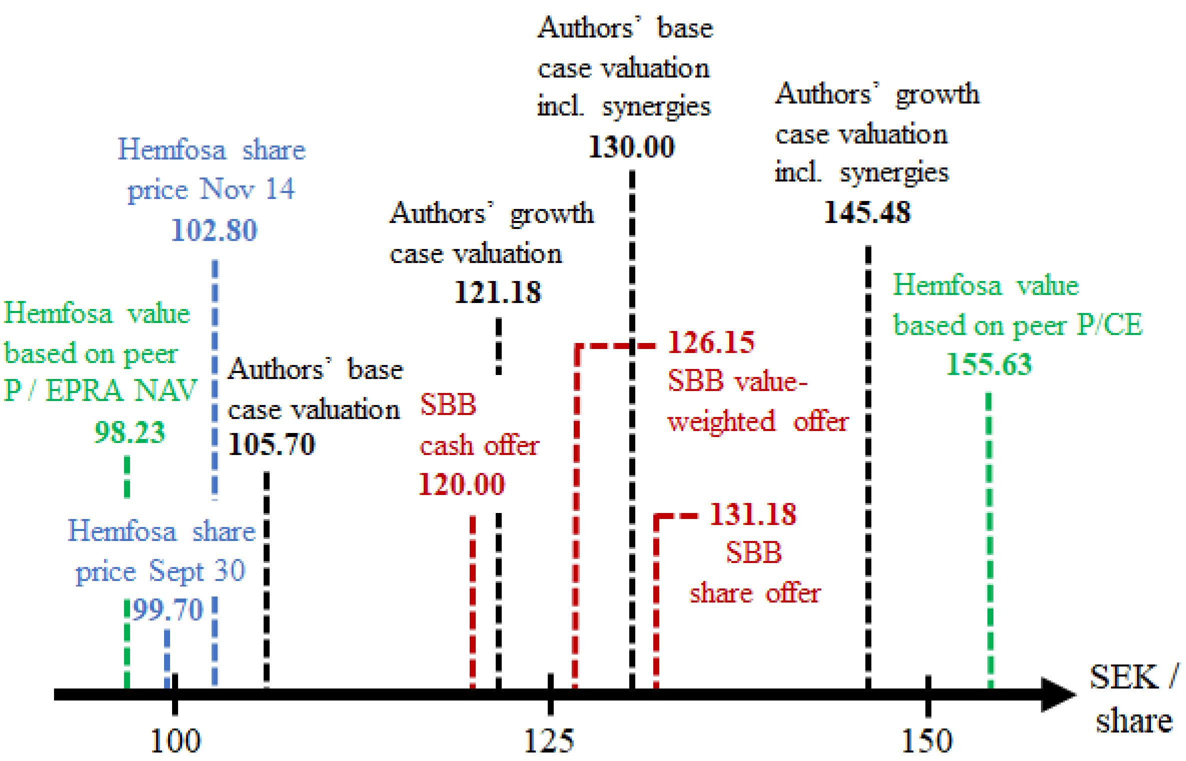
(i) Market capitalization (bn) as of 30.09.2019 = common share value * number of outstanding common shares (Eikon, 2020)
(ii) EPRA NAV (bn) as of 30.09.2019. Long term asset value attributable to common share, adjusted for deferred tax liability and interest rate derivatives. (Source: Companies' interim reports Q3 2019)
(iii) Operating cash flow before changes in net working capital (bn): October 2018 – September 2019 (LTM). (Source: Companies' interim reports Q3 2019)

Hemfosa implied valuation based on peer group median multiples

Hemfosa as of 30.09.2019			
MCAP (common shares)	16.898	*MCAP*	*Per share*
EPRA NAV	14.195	*n/a*	*83.75*
Cash earnings (CE)	1.374	*n/a*	*8.11*
Prevailing P / EPRA NAV	119%	*16.898*	*99.70*
Peer group median	117%	*16.648*	*98.23*
Premium/discount	**2%**	***0.250***	***1.47***
Prevailing P / CE (LTM)	12.30x	*16.898*	*99.70*
Peer group median (LTM)	19.20x	*26.377*	*155.63*
Premium/discount	**-36%**	***-9.479***	***-55.93***

Source: Eikon, 2020; Authors

Summary of valuation, SBB offer and prevailing share prices



Source: Authors

10.14.6 Business description of comparable companies

Company Name	Business Description
Samhallsbyggnadsbolaget I Norden AB	Samhallsbyggnadsbolaget i Norden AB, is a Sweden-based company, which owns community properties in the Nordic region, as well as rental apartments in Sweden. It cooperates with municipalities and other tenants on a long-term basis.
Fabege AB	Fabege AB is a Sweden-based property company active within the area of commercial premises and property development. It is engaged in letting and managing office, retail, warehouses and other premises. It focuses on a number of submarkets in the Stockholm region, including the primary markets of Stockholm inner city, Solna and Hammarby Sjostad. The Company's operational organization consists of three business areas: Property Management, Property Development and Transaction. Property Management business area finds premises for customers' requirements. Property Development business area is engaged in the Company's property development projects. Transaction business area is responsible for the acquisitions and sales.
Castellum AB	Castellum AB is a Sweden-based company active within the real estate sector. The Company is engaged in the acquisition, ownership, management and development of property on a long-term basis. The property portfolio of Castellum AB comprises commercial real estate, including offices, public sector properties, warehouses and logistics properties, retail properties and light industry properties, covering approximately 4.3 million square meters of total leasable area. The Company is also involved in the coworking and shared office space sector. Castellum AB operates in approximately 20 cities across Sweden, as well as in Copenhagen, Denmark and Helsinki, Finland.
Kungsleden AB	Kungsleden AB is a Sweden-based company active in the real estate sector. It is engaged in the ownership and management of real estate properties. Its operations are divided into two segments, namely Commercial Properties and Public Properties. The Commercial Properties segment focuses mainly on industrial, warehouse, office and retail real estate. The Public Properties segment, which mainly consists of the 50% ownership of Hemso Fastighets AB, focuses on retirement homes, schools and preschools, as well as properties for the judicial system and properties for the public sector tenants. The property portfolio is concentrated on the three major city regions of Stockholm, Gothenburg and Oresund, and Vasteras, west of Stockholm.
Klovern AB	Klovern AB is a Sweden-based company active in the real estate sector. The Company is primarily engaged in the acquisition, development and management of commercial real estate properties within the areas of business and science parks, small enterprise parks and city properties.
Fastighets AB Balder	Fastighets AB Balder is a Sweden-based company engaged in the acquisition, development and management of residential and commercial real estate. The Company's real estate portfolio is comprised primarily of residential real estate and is located in such cities, as Stockholm, Gothenburg, Lund, Malmo, Norrkoping, as well as in regions outside metropolitan areas of Sweden and in the Copenhagen region in Denmark.
Wihlborgs Fastigheter AB	Wihlborgs Fastigheter AB is a Sweden-based company active within the real estate sector. The Company is engaged in the ownership, management and development of primarily commercial real estate properties in the Swedish cities of Malmo, Lund and Helsingborg, as well as Copenhagen in Denmark. The Company operates two divisions, namely Property Management, which is organized in nine geographically defined sub-areas, and Business Development, which consists of two units: Project & Development, and Transactions. Projects & Development deals with new build and redevelopment projects, as well as procurement, while Transactions manages all the Company's purchases and sales of properties.
Wallenstam AB	Wallenstam AB is a Sweden-based company active in the real estate sector. The Company's primary activity is the acquisition, management and development of both residential and non-residential real estate located in the Stockholm, Gothenburg and Helsingborg areas in Sweden. The Company primarily manages and develops residential properties, as well as offices, shops, industrial buildings and warehouses, among others.

Source: Eikon, 2020