REPORT | Q3 2024

Nordic Financing Strategies 2024

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Global Talent

Can the Nordics remain a stable investment haven amid global shifts?

Editor: Rory Hickman
Designer: Douglas Soldera Junqueira & Mikael Jacob
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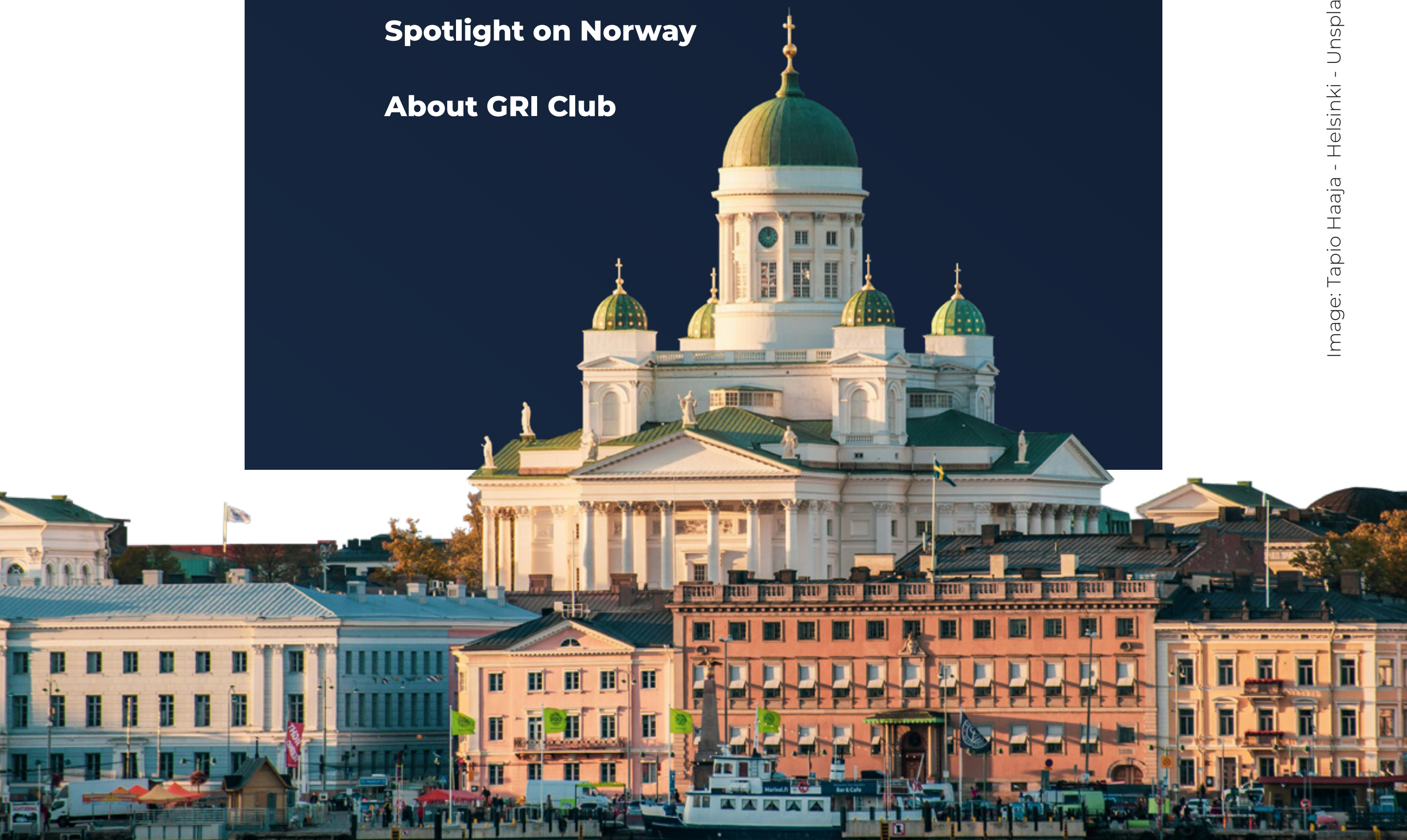
INTERACTIVE TITLES



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INTRODUCTION

For more than 25 years, GRI Club's exclusive networking events have been providing unique opportunities for the industry's decision makers to exchange valuable insights and experiences, igniting deal flow and potentialising the real estate market.

GRI Club reports provide the key takeaways from these events, including the most valuable insights, the most ardent discussions, and the most intriguing strategies.

This report was compiled following the discussion sessions that took place during our inaugural Nordic Financing Club Meeting in Oslo, where senior real estate executives gathered to discuss what to expect from investments in the Nordics region going forward.

The closed-door discussions focused on the Nordic financing and investment market, highlighting the impact of interest rate fluctuations, regional market differences, and the essential role of local partnerships for successful market entry.

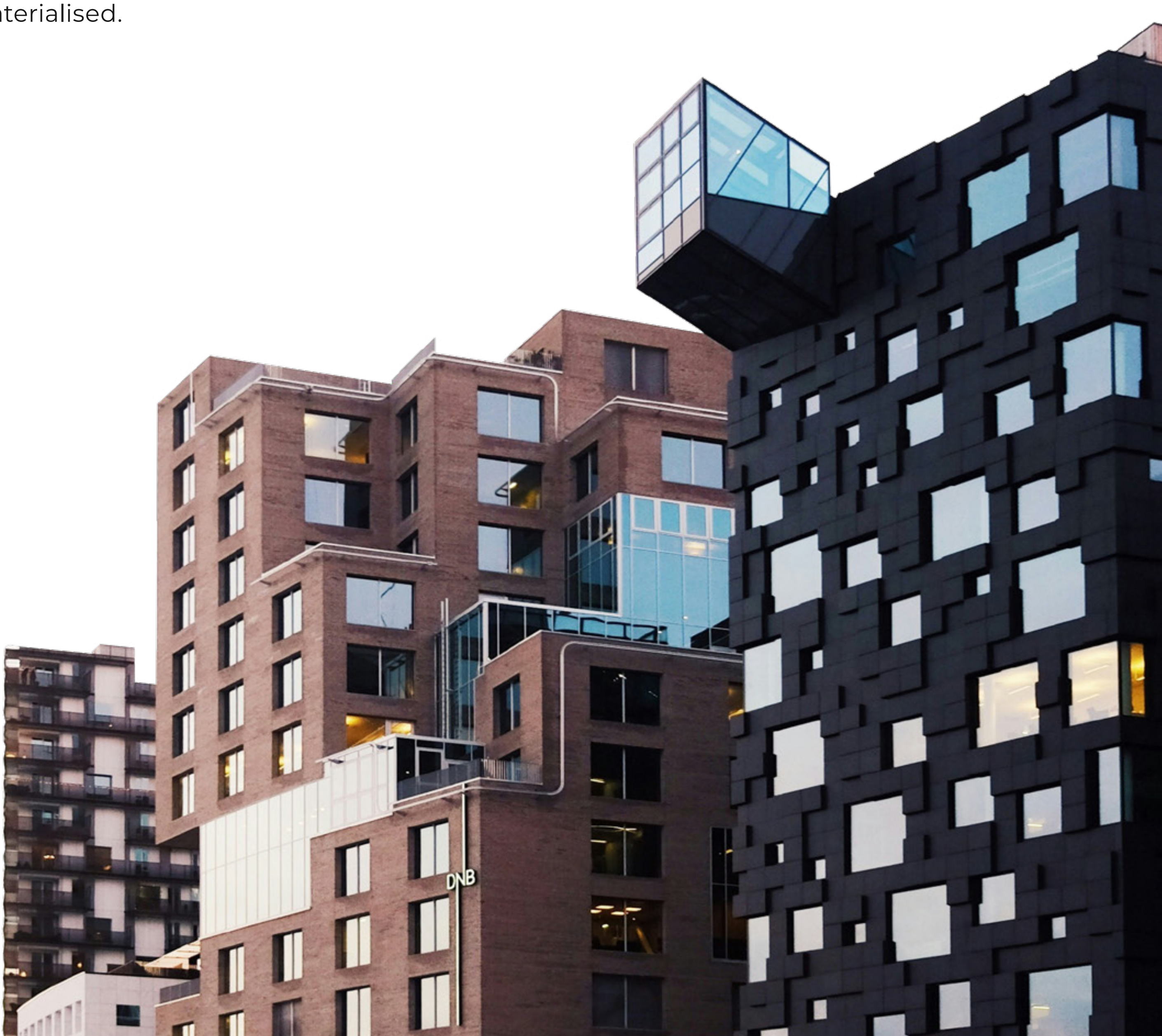
NAVIGATING NORDIC DIFFERENCES

The Nordic markets exhibit notable differences compared to other European and US markets, largely due to distinct societal factors and market dynamics. Successfully navigating this region requires a deep understanding of these unique characteristics.

While often grouped as a single region, the Nordic countries vary significantly in economic and cultural aspects, demanding that investors tailor their strategies to each market's specific conditions, including variations in currencies and regulatory environments.

Norway's market is particularly localised, with domestic investors dominating, which presents barriers for international players attempting to enter.

In contrast, Sweden, being larger and more stable, has attracted attention due to its resilience. However, this stability, shaped by past banking crises, has tempered international investor expectations, as anticipated distressed opportunities have not materialised.



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CHALLENGES IN ACCESSING THE NORDIC MARKET

Accessing the Nordic real estate market has historically been challenging due to local liquidity constraints, but recent decreases in interest rates across the region - except for Norway which has remained the same - have renewed investor interest, particularly in scenarios where structured solutions are viable.

The area is witnessing growing international demand for value-add and opportunistic investments, yet the market's highly localised nature, coupled with liquidity limitations, remains a significant entry barrier for foreign investors, especially in Norway, where domestic players maintain dominance.

Close attention is being paid to current interest rates and the yield gaps between swaps and prime yields, as the narrow yield spreads in the Nordic region complicate the assessment of growth potential and the need for further price corrections.

High construction costs and prevailing market conditions have slowed new development projects, prompting investors to prioritise existing properties with rent uplift potential through targeted investment.

While the rapid changes in interest rates have introduced more complexities, the overall result appears to be the emergence of greater stability. However, for sustained market activity, further rate adjustments may be required.

Encouraging trends, such as increased capital availability from funds and pension investors, bring a degree of optimism, though a cautious outlook persists in the broader market.

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IMPORTANCE OF LOCAL PARTNERSHIPS

Local partnerships play a pivotal role in successfully navigating the complexities of the Nordic real estate market. In an environment marked by uncertainty, investors are increasingly prioritising strategic relationships to unlock opportunities and mitigate risks.

While international debt funds are gradually entering the Nordic markets, they remain behind equity investments, and gaining a foothold often requires smaller deal sizes and close collaboration with local partners, given the market's unsuitability for large, single-asset loans.

For international investors, particularly those dealing with larger investments, teaming up with local players is crucial for navigating the intricacies of the region. The combination of international capital with localised market knowledge and operational expertise is often the key to success.

Image: Tom Brunberg - Helsinki - Unsplash

UNCERTAINTY IN PROPERTY VALUATIONS, MARKET PRICING, AND EXIT YIELDS

The stability of property prices remains uncertain, with ongoing debate over whether further adjustments are needed. Although interest rates may have peaked, valuation challenges persist, creating difficulty for investors in assessing market conditions.

Pricing and yield gaps are being closely scrutinised, as they have tightened compared to historical norms. Even minor shifts in exit yields could have a significant impact on returns, heightening investor caution.

Transaction volumes have slowed overall over recent years, but activity has continued in smaller deals, particularly within the residential sector. Despite current pricing difficulties, some investors are strategically positioning themselves in expectation of improved opportunities as the market eventually stabilises and rebounds.

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INVESTMENT SENTIMENT AND SECTOR ACTIVITY

The COVID-19 pandemic resulted in a sharp decline in new developments, leading to a significant reduction in new build volumes over the past few years. This slowdown has contributed to sustained low vacancy rates in major cities.

It was noted that transaction volumes are beginning to recover, particularly in larger deals, creating opportunities for new entrants to capitalise on favourable market dynamics as activity picks up, especially those focused on private debt and pan-European investments.

Despite a subdued broader market, the residential sector remains active with ongoing building and development. Investor sentiment is cautiously optimistic, with opportunities available for those prepared to navigate a more complex environment.

Core investment opportunities are limited, with low participation from international core investors. Instead, value-add and opportunistic strategies are gaining traction as they offer better prospects in the current financing landscape.

The current market conditions present a rare opportunity for foreign buyers to acquire assets that would typically be dominated by local buyers in a stable market. With local players facing financial constraints, international investors have a brief window to secure attractive deals.

After prolonged uncertainty, market sentiment is gradually improving, and confidence is returning as conditions stabilise. While caution persists, especially with lingering global unpredictability, there is a growing sense that the market is moving in a positive direction.

Increased regional predictability within the Nordics, particularly compared to earlier periods marked by highly volatile construction costs and interest rates, is contributing to this renewed confidence.

NORDIC INVESTMENT STRATEGIES

Investment strategies in the Nordic region are evolving, with a growing emphasis on equity plays as market conditions stabilise. Despite recent fluctuations in interest rates, there is optimism that Norway's equity market will recover more swiftly than expected, underpinned by the market's inherent strength.

The debt market in the Nordics is also undergoing change, with increasing demand for private debt and non-traditional financing solutions. This shift is driven by a changing macroeconomic landscape and the need for alternatives to conventional bank financing.

Nordic banks have upheld conservative financing practices, such as requiring high pre-rent ratios before new projects can proceed, which has played a key role in maintaining stability and low vacancy rates across the region.

In addition, Nordic banks have remained cautious in their lending, keeping loan-loss provisions low and thereby reinforcing the stability of the financial environment despite recent economic pressures.

As traditional bank financing remains primarily geared towards local investors and large property companies, there is a growing need for private credit solutions. This presents an opportunity for international credit funds to enter the market and address the gap, particularly through strategic partnerships.

Image: Jon Flobrant - Stockholm - Unsplash

TOP TRENDS IN THE NORDICS

Repositioning and Redeveloping Assets

There is growing interest in repositioning older buildings, particularly within the hospitality and residential sectors. This approach is increasingly recognised as a viable entry strategy for underperforming assets and has been successful in several cities across Europe.

Hospitality Sector Dynamics

The hospitality sector is viewed as a high-risk, high-reward asset class, particularly appealing during periods of economic uncertainty. Investors with in-depth market knowledge can achieve strong returns.

However, following the COVID-19 pandemic, investment has shifted towards core city locations, while fringe areas have become less attractive. Entering the Nordic hospitality market remains challenging without local expertise or partnerships, as hotel assets are typically traded within established networks.

Emerging Interest in Data Centres

With major tech giants like Google, Microsoft, Meta, and Amazon having already established a strong presence in the region, data centres are rapidly gaining prominence as a key asset class in the Nordics. Along with political stability, advanced digital infrastructure, and strong government support, its strategic location also offers excellent connectivity to major European markets, enabling low-latency data transfers.

The region is considered to be ideal for data centres due to its cool climate, reducing cooling costs, and abundant renewable energy sources, which ensure stable and sustainable operations. It was noted that the growing focus on ESG compliance and regulations like CSRD (Corporate Sustainability Reporting Directive) is making due diligence and real estate compliance increasingly crucial in transactions involving data centres.

Sustainability in Commercial vs. Residential Real Estate

Sustainability is becoming a major focus, particularly in commercial real estate. While residential end-users are not yet willing to pay a premium for green apartments, large corporations are increasingly demanding environmentally compliant office spaces.

This trend is driven by regulations such as CSRD and the EU taxonomy, which require businesses to report on carbon footprints, thereby prioritising green buildings.

SPOTLIGHT ON NORWAY

The high interest rates in Norway, currently at a 16-year peak, are putting additional pressure on the market. Despite differences from the broader European zone, investment interest remains strong, though navigating the local market remains challenging.

The Norwegian market, less crowded due to local financing constraints, offers an appealing entry point for international investors. With many local players at a standstill, international investors with available capital have an opportunity to step in.

Norway's property market has shown resilience, underpinned by stable top-line performance even during difficult periods. Compared to previous financial crises, the current environment is more stable, with positive momentum expected to persist, particularly in equity investments.

The market fundamentals, especially in Oslo, remain robust. Low vacancy rates, limited new build activity, and disciplined financing practices have created a stable supply-demand balance, which continues to support revenue growth despite tight spreads.

Image: Damon Zaidmus - Oslo - Unsplash

NORWEGIAN ASSETS

Office and residential assets are prioritised in the current environment due to strong demand and limited new developments. Norway's population growth and favourable demographics further reinforce the residential sector.

Despite high interest rates, the residential market remains strong, with local buyers returning and high-end projects performing well. However, challenging zoning regulations are expected to lead to a supply shortage in the coming years, driving additional demand.

In Oslo, the office market remains solid, with demand rebounding well after the pandemic. The focus has shifted towards centrally located, environmentally friendly spaces, as companies increasingly prioritise sustainability.

While vacancy rates are low, new developments face significant challenges due to persistently high construction costs and yields, making it difficult to launch new projects. Although starting new projects remains challenging across the Nordic region, demand for well-located, sustainable office spaces continues to keep the leasing market active.

This situation has resulted in a growing preference for leasing existing spaces. The refurbishment of these existing properties is also gaining traction, driven by the growing environmental focus of companies in Norway. Tenants are prioritising reducing carbon footprints and aligning their offices with sustainability objectives.

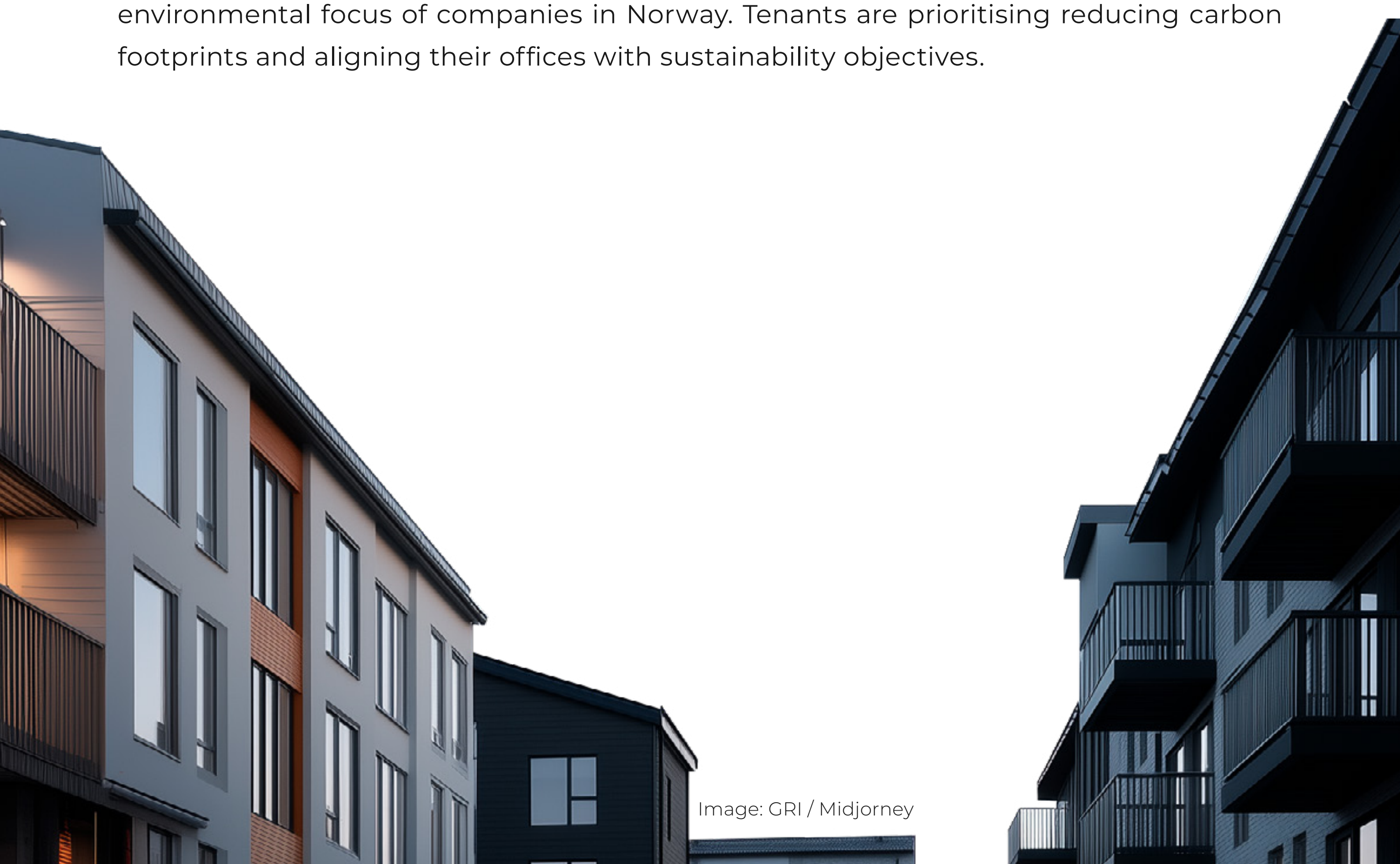

Image: GRI / Midjorney

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CAPITAL CONNECTORS FORUM: UK - NORDICS - GERMANY

GRI Club

Founded in 1998 in London, GRI Club currently brings together more than 17,000 senior executives spread across 100 countries, operating in both real estate and infrastructure markets.

GRI Club's innovative discussion model allows free participation of all executives, encouraging the exchange of experiences and knowledge, networking and business generation.

GRI Club Members also have access to our exclusive online platform to learn more about other members and their companies, correspond and schedule meetings, and receive unrestricted access to all GRI Club content.

Find out more about GRI Club Europe.

CONTACT

Diego Tavares
Managing Director & Senior Partner
diego.tavares@griclub.org

Kirsty Stevens
UK & Pan-Europe Director
kirsty.stevens@griclub.org

GRI Club

GRI Club Europe   GRI Club   @griclub.europe

griclub.org

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