

# Full Regular Transcription

## Heimstaden Bostad

### Q3 2024 Results Conference Call

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#### COMPANY REPRESENTATIVES

Helge Krogsbøl, Co-CEO

Thomas Hansen, CFO

Paul Spina, Chief Management & Sustainability Officer

Christian Fladeland, Co-CEO

## PRESENTATION

### **Krogsbøl Helge**

Welcome, everyone, and thank you for joining us for the presentation of the Heimstaden Bostad report for the third quarter of 2024. I'm Helge Krogsbøl, co-CEO of Heimstaden. Together me, joining the call is co-CEO, Christian Fladeland, CFO, Thomas Hansen, and Chief of Asset Management and Sustainability, Paul Spina.

I would like to inform all participants that this presentation is intended only for investors and other financial stakeholders. As per usual, today's speakers will go through a management presentation before we open to questions. Questions can be asked on the phone or in writing via the webcast. We will only address questions on Heimstaden Bostad. If you have additional questions after the call, especially if your inquiry is modelling related, please reach out to our investor relations team after the call.

Then I will reach over to some highlights from Q3. We again see increasingly strong underlying fundamentals as like-for-like rental growth improved to 6.3%, which is well above the blended core CPI of 2.1%. The NOI margin on a last 12-month basis increased to 69.3, which is an improvement from 66.2% in Q3 last year. This is the 11th consecutive quarter of NOI improvement. We're also pleased with a record NOI of 73.1%, which outperformed other previous record setting from Q2 figures of 71.5.

Property values on a fair-value basis have returned to organic growth with that productive quarter-over-quarter growth of 0.8% as compared to 0.4% last quarter. Christian will comment further in valuations and expectations later in the presentation.

Finally, the privatisation plan continues to track on schedule as we continue to deliver, with cumulative sales of 6.4 billion SEK gross sales. Gross premium remained strong at 27.9%. For those following on a quarterly level, this entails 516 sold units at a total sales value of SEK 2.4 billion. Premium to book were at 24.6% for Q3 standalone and SEK 1.6 billion of net proceeds for liability management.

With that, I now hand it over to Thomas, who will give a brief update on the figures.

## Hansen Thomas

Real economic occupancy improved to 98.7% for the quarter, from 98.3% in Q2. Per outlook publication in Q2, we continue to expect occupancy to remain above 98%. As seen in previous quarters, the strong real economic occupancy trend in our regulated markets sustained, especially in Germany and Sweden, as both improved to 99.8 and 99.2% from 99.7 and 98.9% respectively.

Denmark has seen six consecutive quarters of occupancy improvement from 96.6% in Q1-23 to 98.8% in Q3-24. We continue to expect these levels as the underlying supply and demand imbalance persists.

Poland was again impacted by the delivery of new assets. The portfolio saw a quarterly gain to 89.9% from 86%. Specifically, we received 340 new units as compared to 693 new units in Q2, and we're expecting another 329 units to be delivered in Q4. Our occupancy remains compressed due to the delivery of new assets. We have seen impressive commercialisation of the new assets in recent months, contributing to the increase since the last quarter.

Like-for-like rental income growth was on a 6.3% increase over our comparable portfolio from a year before. The comparable portfolio now represents 97% of total rental income. Our blended core CPI benchmark continues to decline to 2.1% from 4.3% a year ago. This then marks the fourth quarter of like-for-like growth surpassing inflation, showcasing the possibility for rents to outperform CPI over time.

For Sweden we observed another strong level of 5.9%, which is well above the local CPI of 1.3%. This is due to a combination of the negotiated rent increases and our tenant improvement programme. Rental growth is driven by annual negotiations with local tenant associations and business plan execution, including value-add capex such as apartment upgrades. Looking ahead, we will benefit from two-year agreements from 2024, with rent indexations between 4.5 and 5%.

Germany posted a strong result with a quarterly figure of 7%. This growth can be attributed to rent reversion to market rent upon tenant churn, increased occupancy and tenant improvements. UK had most of their portfolio delivered in Q3-23, so this like-for-like growth mainly represents the year-over-year ramp up of letting the new assets.

Our NOI margin improved as we saw growth to 69.3% from 68.4% on the last 12-month basis. Our quarterly margin improved to 73.1% versus 69.6% a year ago.

Outside of the income gains, further driving the margin development is a continuation of our cost control measures, which resulted in a flat cost development on our property expenses on the last 12-month basis. Our aim is to continue to perpetuate the imbalance between rental trends and cost basis. We expect the full year margin to outperform the outlook range, given our strong year-to-date performance.

I now hand it over to Paul.

### **Spina Paul**

Thanks. I'm taking a deeper dive into privatisation where the plan remains profitably ahead of target year-to-date and well on track for our 20 billion SEK sales goal by 2025. Looking at the results in Q3 isolated, we sold 2.4 billion SEK in sales value at 24.5% gross premium. That equates to 213 million SEK in net profit and 2.1 billion in total proceeds for debt repayment. Of that, about one quarter or 534 million SEK is asset-backed, secured asset-level financing and 75% for capital markets repayment.

Overall, the KPIs on the plan remain exactly as forecasted at gross premiums of 27.9%, net premiums of 13.2, total proceeds for debt repayment 5.6 billion SEK, and all of that on an implied yield of 2.9%.

Denmark and Netherlands are now out of the ramp-up phase and approach full stabilisation, where we expect to be able to continue with similar results looking forward in both of those countries, even with some upside as we bring a few final assets online into the programme.

Norway started sales over the summer as planned and contributed with about 85 units at 400 million SEK in sales value. We now continue to ramp up over the next three quarters, with volumes growing consistently before full stabilisation there in Norway. The ramp up plan in Norway is focussed on making assets ready for sales and structured from a physical perspective as well. Inventory is not a problem as we see collective churn strategically and see an incredible demand in that market as well.

Capital allocation remains the key priority for the business, while the effects of our increased hurdle rate continue to funnel through with 38% reduced capex on standing assets year-over-year. That's 43% down on tenant improvements, 75% down on value add, while in sustainability capex we see a slight increase linear year-on-year based on attractive risk-adjusted returns, as well as steady alignment with our climate roadmap goals.

The effect of our repair versus replace mantra continues to hold true with our maintenance capex fall, delivering about 38% reduction in spend year-over-year.

Then combining both of those two topics and showing here an internal metric that we use to measure the effects of prioritising cash generation across the business. One thing that we do internally is compare NOI and net proceeds from privatisation versus overall outgoing cash for capex.

In 2022, when the business was just on the back of a heavy investment and growth period, we showed a negative 8 billion SEK in this metric with NOI and net proceeds of 6.1 billion SEK. Over the last few years, we've improved that by 14.5 billion SEK, now with 11.4 billion in NOI, plus net proceeds from privatisations, less 4.9 billion in capex and development. This, of course, shows that the business has high optionality, and while it takes time, the majority of today's effects and results are based on decisions and strategy changes from 2022, in the middle of the year, flowing through to now, midyear 24.

With that, I think I can hand it to Christian.

#### **Fladeland Christian 00:10:48**

Thank you, Paul. Fair values continued to recover over the course of Q3 2024. On an aggregated basis, we experienced a 0.8% value growth. We had four markets that was essentially flat, plus minus 0.5%.

Germany we see that yields have started to stabilise and the operating environment is continuing to dominate. Even though yields are still expanding moderately, we do see that values have stabilised, given that NOI continues to improve. In the Czech Republic we continue to see stronger occupancy rates, we continue to see rental growth, while yields are still expanding a bit, even though central bank rates have now stabilised and have come down quite a bit from the peak.

In Norway we have seen that the ownership housing market was very strong in the first half of 2024. We see that it calmed down a bit here in Q3, reflecting most of all seasonality [unclear 00:11:46]. For the same reason, we also anticipate that this stabilisation, which has a slight negative sequence in front of it, is something that will only be temporary. In Denmark, we were marginally up, reflecting the improved operating market environment and stable yields.

On the markets that show more impressive value growth in the quarter, it's worth highlighting the Netherlands, UK and Poland.

The Netherlands continue to see a lot of tailwind from the strong ownership housing market, which was driving continued ownership housing value growth. In addition to that, we saw increased investor activity within the privatisation business plans. That provides better clarity on the cost of capital for these business plans. It's also supportive for the valuation and we ended the quarter with almost 5% value growth quarter-over-quarter.

In UK and Poland, the dynamics are quite similar. It's unregulated market, whether it's in dividend, housing shortage, and with the short-term leases, you're able to very quickly regear those at higher levels. So, the tailwinds that we are getting from higher market rents there has supported valuations, while yields have been remaining flat.

You will notice a quite steep decline in the NOI yield from Q2-24 to Q3-24 for Poland, which doesn't reflect our valuation yield compression, but it reflects that we have taken over a newly built in Poland late in the quarter, which means that even though occupancy rates in Poland across the quarter has improved from Q2 to Q3, as of the balance sheet date, there was higher vacancies, which is reflected in a lower NOI yield. Next quarter, we are very certain that you will see a recovery in that NOI yield from a valuation perspective and it will revert to the 5.7, 5.8%, all else equal, assuming no change in market conditions.

In Finland, we saw a significant improvement of the operating performance of our portfolio. It's a market that has attracted a lot of attention in recent years due to the excess supply. We see that for our locations, that the operating environment has evidently improved. We can see that both in the occupancy rate, but also our ability to grow like-for-like rents.

In Sweden, yields have been stabilising on the back of the first six market interest rate cuts and we anticipate that to continue. In the meantime, we continue to get more clarity on the negotiated rental increases forward looking, and that is looking more positive than previously, and that's the value that's taken into account. All in all, this led to a 2.6 billion SEK increase quarter-over-quarter.

During the quarter, we spent 746 million in capex in existing assets, 429 million in relation to the new build pipeline. We divested 1.8 billion SEK, mainly relating to the privatisation schemes and some smaller investment property sales. Then we have sold per the quarter-end date 224 million SEK of assets, which have been unconditionally sold, but not yet transferred, meaning that they will be reclassified to assets held for sale. Then we finally had negative FX impact of 1.4 billion SEK, reflecting that the SEK closed the quarter stronger against most of our other currencies, in particular, the euro.

Looking into the fourth quarter of 2024, capital markets have continued to improve and we see that that may open up for diversifying our funding mix. We made our first entry back to the bond market for two and a half years late August, early September with 2.4 billion SEK of bonds issued in total. We have now this morning launched that we will start to investigate whether there is a potential to do a Eurobond offering and re-enter the euro market for the first time since January of 2022. We sent out an invitation to sign up for investor calls on Monday, and I encourage all of you to, of course, reach out if you want to participate.

We think that margins now have come down to a level where, even though it is still elevated compared to the peer group that we believe we should be compared to, it is still a level where it makes sense to consider diversifying our access to capital and also start to build the [unclear 00:16:05]. We also believe that Q4 will continue to show strong recovery of residential values. Most importantly, we believe it will be driven by continued strong operating fundamentals.

The plus 6% like-for-like rental growth that we have experienced in this quarter is something that is really underpinning that you will be able to see continued yield expansion to accommodate to the existing interest rate environment, while still be able to grow values. That is what we refer to as sustainable value growth. On top of that, we also believe that the interest rate cutting cycle is something that will continue to support the yield requirement development, and we see additional upside for that if it stabilises and even may compress in some markets.

In relation to our overall expectations and the outlook that we have previously communicated in relation to key metrics, that being ICR, LTV guidance, all the operating figures, we believe that we will remain within those ranges. Alternatively, we might see some upside in some of those, but it's not something that we're willing to guide on now.

As of now, we believe that we're on track to deliver on the targets that we have set for 2024 and likely also a bit better than that. With that, I want to open up for Q&A.

## QUESTION & ANSWER

### Operator

We will now begin the question-and-answer session. Anyone who wishes to ask a question or make a comment may press star and one on their touchtone telephone. You will hear a tone to confirm that you have entered the queue. If you wish to remove yourself from the question queue, you may press star and two. Participants are requested to use only handsets when asking a question. Anyone who has a question may press star and one at this time.

Our first question comes from the line of Neeraj Kumar, Barclays. Please go ahead.

**Kumar Neeraj**

Morning, everyone. My first question is with regards to your hybrids. Given the rally in hybrids, is it possible to see a new issue hybrid from you coming out of the blue or do you plan to stick to the conventional exchange route?

**Fladeland Christian**

Hi, Neeraj. I would say that we haven't concluded on how we will handle the hybrids for the reason that you also allude to. We have been looking at the benchmark transactions in the market with a lot of interest and something that we are definitely considering. At the same time, we also see that our hybrid is closing very much in on par and the market has changed significantly.

You will not be able to get me to communicate anything concretely in this respect. The only thing I can say is that we want to do something that is as close as possible to the reset date, as we want to make sure that we are supporting the ICR as much as possible.

**Kumar Neeraj**

Perfect. I'll try once again. You said you want to do it closer to the reset date, so that's not something you're looking to do before the S&P review in December. Is that something you need to do for them to give you a stable outlook and is that the timeline you're targeting for the stable outlook from them?

**Fladeland Christian**

It's not like S&P is giving us the recipe for how to get rid of the negative outlook. I believe that S&P would understand that we are focusing on protecting the ICR metric. We will lay out what we assume is our financial forecast with our annual review with S&P and then we would evaluate the actual plan when we get closer to the reset date.

That is our plan as of now and we have not decided on anything firmly, whether it could be one of the benchmark transaction structures that we have seen, whether the market would be strong enough to do a new issuance. That we have to evaluate when we get closer.

**Kumar Neeraj**

Got it. I'll move on to the privatisation. Can you help us with the magnitude beyond 2025, as in, how much do you plan to sell, let's say, in 2026 or so?

**Spina Paul**

We haven't publicly announced, but the intention is to continue through. I think that this time last year we outlined a total sales perimeter of 80 billion SEK. Of course, as we continue to sell, then there's less inventory to sell. But we would expect 26 at this point in time to look similar to 25.

**Kumar Neeraj**

Got it. If I may ask a bit of a controversial question here. Given the improved access to the financing and the pace of the privatisation programme, do you think there is a need to look at the large-scale disposals or new equity, for that matter, to deleverage?

**Fladeland Christian**

We have a very disciplined approach to disposals. We've also communicated earlier that we are looking at doing additional disposals, but it has never been with the intention to do something for just saving the rating. We believe the current plan with privatisations are fully sufficient to safeguard the investment grade rating. However, we do also believe that the company would benefit from an even more advanced deleveraging path. That is always at the trade off at what terms we can do the transactions.

Even though that there has been several tailwinds that are supporting our credit metrics, even on an all-else-equal privatisation plan, at this situation, we still think that it would make sense to advance the deleveraging pace. But, of course, we are looking at market dynamics and want to make sure that we get well paid before we are entering into any additional transactions.

**Kumar Neeraj**

Got it. Probably the last question from my side. You mentioned you think the spreads are still elevated compared to the peers. May I know who do you think is the peer at current rating levels?

**Fladeland Christian**

I don't think that our rating level either corresponds to our risk profile, so this is an even more philosophical question. I think that we should definitely be at least a B minus with stable outlook. When you look at our underlying risk profile and the flexibility of our balance sheet, I would even say that we would be very positive within that parameter.

You have other residential landlords, which I don't need to mention by name, that will be minus stable, and then you also have some other that is in the BB bracket, which I have sympathy, we might need to trade slightly higher. But then that gap is also quite large at present.

**Kumar Neeraj**

Got it. Thank you very much and good luck for the new year.

**Fladeland Christian**

Thank you very much, Neeraj.

**Operator**

The next question comes from the line of Noor Sehur from Morgan Stanley. Please go ahead.

**Sehur Noor**

I have a question. Just one follow up for me. Neeraj asked most of the questions. On the larger disposals, I think when we met last time, you mentioned that you guys may be close to announcing something in Q4. Just if you can give some colour around that. What are you guys seeing in the transaction market? Has there been any progress in any of these disposals that you're closer to? That's about it.

**Fladeland Christian**

First and foremost, in terms of larger disposals, it's important to emphasise that it's not larger in the context of our balance sheet, but it's not privatisation individual unit sales. We have transactions in due diligence that is of institutional size character. That is not €200, €300 or €400 million transactions, but still decent in size, and we still anticipate that will conclude within the coming quarter or so.

It's important to navigate what is meant by larger. You should not anticipate that there will be announced a €300, €400 or €500 million transaction within a month or two, but there could be a series of traditional institutional sized transactions and they're progressing.

**Sehur Noor**

On the secured debt question, what are the spreads, latest spreads that you guys are getting secured that are...? Just so I understand when you say now you're issuing a bond. It would be interesting to understand what level you're getting in the secured debt market.

**Fladeland Christian**

We have been doing secured debt anywhere between 70 basis points and to 200 basis points in the last quarter for the traditional, long-term hold portfolios. That, of course, with the banking market in the CEE is more expensive than Danish mortgages, which is the two harder points in this range.

Then we are doing some specialised, more flexible, fixed facilities related to the privatisation part of the portfolio where you need to have big prepayment flexibility, i.e. no prepayment fees and a more flexible outstanding amount, and there is typically a bit different price dynamic. But for the ordinary, long-term hold financing, which is what we are benchmarking potential access to the capital markets with, it will be between 70 and up to 200 basis points.

### **Sehur Noor**

Thank you. That's all.

### **Operator**

The next question comes from the line of Mary Pollock, CreditSights. Please go ahead.

### **Pollock Mary**

Hi. Thanks for taking the questions. I think there's really a lot to be positive about here. I wonder, when we're starting to think about 25, how are you thinking about capex next year? There's clearly a lot of value accretive things you could be doing with regards to your existing portfolio. How can we expect capex to change into next year? Similarly, can you provide any context about the dividend for 2024? Is there any chance the pref A is reinstated or pref B or any of the other dividends? Thanks.

### **Spina Paul**

Why don't I start on the capex and then Christian can take the dividend part? I think the beauty of our capex programme is the flexibility in it. When you look at something like tenant improvements, those can be made on the fly at any point in the year.

Our base case next year is that capex looks relatively flat compared to this year. Maybe there's a similar trend of slightly increased sustainability capex. But from a maintenance, tenant improvement and value-add perspective, our forecast is roughly flat. We have our yield hurdle rate at 10%. I think we'd be really excited to deploy capex above 10%. Overall, there are some opportunities, but I wouldn't expect a significant increase there.

### **Fladeland Christian**

Maybe just to add to that, we tightened the capex threshold to 10%, as Paul also referred to, on the basis that let's assume that the most expensive marginal funding that we had at any point in time was around 5% when you had the swap curve above 3% for most centres and then the most

expensive asset-backed funding margin on top of that, and in order for that to be ICR accretive, we needed to get to 10%.

Now, where the absolute most expensive marginal funding for long-term financing is typically four, four and a quarter, then of course there is also a basis for considering lowering that threshold. That might, as Paul also alluded to, mean that we are a bit more flexible in that respect. But still, we do anticipate to keep it flat as of now.

In relation to dividends, it's of course up to the board in the end, but I would be very, very surprised if there were any dividends on the table for 2024. There is one target, and that is to stabilise the rating, get rid of the negative outlook, and also set a path for getting back to our BB flat rating in the coming years.

**Pollock Mary**

Thank you.

**Operator**

As a reminder, if you wish to register for a question, please press star and one on your telephone. Star followed by one. Our next question comes from the line of Othman El Iraki, Fidelity International. Please go ahead. Othman El Iraki, your line is open. You may ask your question.

**El Iraki Othman**

Yes, sorry, I had some tech issues. Actually, my question was already asked by Neeraj, but maybe just a follow up to that. Given the fact that your spreads are, you have touched a lot on the senior side and the reset on the hybrid, the one coming up, are relatively high, actually, is it fair to say that maybe issuing a brand-new hybrid now is in your toolkit or do you think your ICR is still tight to envisage something like that? Thanks.

**Fladeland Christian**

I think we need to see the basis for a new hybrid issuance that would not be ICR decreative [? 00:29:24] compared to our alternatives. I still think that that is such an important metric for us to stabilise.

That being said, it's something that I need to get used to referring to, because now I have been navigating a complete different environment for the last 12 to 18 months. But with the hybrids getting very close to par, they are coming, one that is the reset in February 2025.

It's of course something that we need to follow very closely and see whether that could also be a realistic part of the toolbox as we close in on the reset date.

**El Iraki Othman**

Makes sense. Thank you.

**Operator**

Ladies and Gentlemen, we have no more questions.

**Fladeland Christian**

I believe...

**Operator**

Sorry, go ahead.

**Fladeland Christian**

I would just say that I understand that there is no more questions, but you were ahead of me. If that is the case, then I thank everybody for participating. I look very much forward to speak with many of you on Monday. Wishing you all a great weekend.

- END -