



The Nordic Investor Podcast

Transcript

Episode 1: Q1/21

Tomas Hildebrandt: Hello and welcome to the Nordic Investment Podcast for professional investors. My name is Tomas Hildebrandt and I will be your host for this new series on the Nordic market outlook set the run over the course of the year. I'm the market strategist at Evli's institutional asset management in Helsinki.

Every quarter we will present a short-term outlook for the Nordic market, review learnings from the previous quarter, examine changing cross-asset trends and highlight key things to keep an eye on. And as is the case with everything we do at Evli, sustainability and ESG will remain central in our thoughts.

Today, joining me for this first episode are Sauli Vilén, who is the Chief Equity Research Analyst at Inderes and my colleague Jukka Hyvönen, who is the Sales Executive in our Stockholm office. Gentlemen, welcome to the Evli Nordic Investment Podcast. Nice to have you here.

Jukka, you have been working for a long, long time on the bond markets and you have been living in Stockholm for a very long time. It seems that you really love your job and love Stockholm.

Jukka: Yes. Actually, I ended up here in the late '90s, in 99. The idea was to get experience for two to five years, but it has been a little longer time. And I think it will be a few years more, to be honest. I'm enjoying working and living in Stockholm, even though nowadays visiting Finland, for example, is not that easy due to the restrictions, but I hope things are getting better. As you mentioned, I've been involved with bonds for quite a long time and I've been working for one decade in Finland and two decades here in Stockholm. More or less, most of my career with fixed income, especially investment-grade and high-yield bonds, sales and trade.

Tomas: Okay, let's go to the topics of today and start by talking about the beginning of 2021. We have the Coronavirus still raging on globally, we have remote working as you said, Jukka, impacting many businesses and many, many companies. But apart from that, there's some optimism in the air and many are hopeful that this

recovery will continue, and we will get back to normality within this year. So, gentlemen, how would you expect the market to evolve in this kind of environment and what factors would you look at? Would you like to start, Sauli?

Sauli: I think the main question is that what kind of economy are we leaving when we have finally defeated Corona, in H2, basically. The stimulus has been so huge from the central banks and also from the government side that it's kind of difficult to see in what state the underlying economy is at the moment and when do we finally beat the virus. That step is the key question and that will drive the earnings of companies.

Tomas: So, it's the revival of consumption. The industry has bounced already quite nicely and in many of the Nordic countries the industry and industrial companies are quite dominant, so it has shown in the economic performance here.

Sauli: Yes, it will obviously be how the consumption will develop after this. And obviously, inflation will be one key topic to closely follow in the upcoming quarters. How will this totally new way of stimulating the economy affect inflation? If we would see inflation, it would put pressure on bond yields or the central bank rates. Forecasting the economy at the moment is super, super difficult due to all these factors.

Jukka: It's quite interesting that you mentioned inflation. Inflation is coming up in quite a few comments and financial newspapers. It's quite controversial that Riksbanken has announced that the rates are going to stay until 2024 and that inflation is going to be pretty subdued. It's kind of difficult to say. At the same time, you are talking about the possibility of inflation and maybe higher rates, and simultaneously the central bank here in Sweden is saying that that's maybe not the case and they will have to accommodate the industry rates for a long time. And that would maybe support the economy. It's a little bit like you have a patient that is taking medicine and is getting better, but you don't know when you can take the medicine away.

Tomas: Now we have a really tough question from our French TPM and I would like now to ask it from you guys: So why would anyone invest in Nordic companies when they are already included in their time pan-European investments or in the index?

Sauli: In the Nordics, our banking sector is super robust, I think it's definitely strongest in Europe and I guess it's competing with the strongest in the world, actually. So you don't have to take that legacy with you if you invest in the Nordics. Our economies are in better shape than in Europe overall, the prospects are better, just to name a few.

Tomas: During the past year Finnish smaller companies have really been rallying so do you expect this rally to continue?

Sauli: Well, in the broader perspective, I believe this rally is based on the fundamentals since we have lots and lots of super interesting companies in the small/mid-cap space in the Nordics. Some of them are tech-driven and some of them might be ESG-driven. We have a lot of interesting companies which are already maybe so-called local champions but there are tons of companies which have the potential to be global champions, also. We really like that small/mid-cap space at the moment in the Nordics and that definitely should be a place for investors to watch.

Tomas: That's an exposure you get when you're investing in the Nordic markets.

Sauli: Yeah, definitely. If we can continue on the exposure thing, the stock exchanges in the Nordics are fairly concentrated. For example, our index top 25 companies in Finland: if you buy that, you will take 10% exposure on a couple of names, basically. You need to take a massive exposure on individual names.

Tomas: I think the same thing is in the Danish market as well.

Sauli: Yes, the same thing. And the same thing is in Sweden. Correct me if I'm wrong, Jukka.

Jukka: Well, I would say that the market is somewhat broader here, so can't really comment on that directly.

Sauli: Yes, but my point is that if you buy Nordic straight through your indexes you are actually taking a kind of heavy exposure for individual names or companies.

Jukka: That's true, yes.

Sauli: And that leaves you kind of a small exposure for the local champions and those up and coming names there for example in mid-cap space. Thereby, I don't think the best way to invest in the Nordics is through index funds since our index structures are very different if you compare them with S&P 500 or Eurostock 600. You don't get diversification there, basically, and you are exposing yourself to individual names heavily.

Jukka: That's true.

Sauli: That's why - obviously since I am an equity research analyst I have to say this - I believe I can create Alpha in the Nordic equity space since our market is not as efficient as it is across the Atlantic in the US, for example.

Tomas: Shifting a little bit to bond markets, Jukka, this same issue that Nordic banks are quite dominant in the bond market. But can you find any other segments or niches that are interesting for international investors?

Jukka: In Sweden, there are a lot of issuers from the real estate sector, and there are very, how could I say, different kinds of issuers, so you can take quite high-risk on that segment or you can take a more conservative risk. But the fact is that the Swedish market is dominated by the real estate sector issuers.

Tomas: How is it with these large issuers there, they have of course international ratings, but there's plenty of names in the Nordics that are unrated. And that has to do also with the analyst coverage.

Jukka: That's an interesting question if you compare it to the equity market as well, especially now. Earlier, banks and some brokers gave something which is called "shadow ratings" to the smaller issuers that didn't take the official S&P or Moody's rating. But now when the legislation and rules have changed, the banks and brokers are not allowed to give shadow ratings. Nowadays, it's only the rating agencies that can give a credit rating to the issuer. That has made it a little bit more difficult but simultaneously interesting to invest in good companies that are listed but not rated.

Tomas: How would you Jukka describe the depth of the Nordic Bond markets: are there many domestic buyers and sellers and what about trading activity, size and so on? How does the market function?

Jukka: Well, it's quite a versatile market in the sense that we have four different markets and four currencies - or five currencies, if you count the dollar as a currency, as we all do. So you get quite different kinds of markets. Norway is dominated by the high-yield market and the investor base is quite international for the high-yield companies. But when you come for example to Sweden, there are of course many kinds of issuers: the biggest companies issue in euros and they have ratings and, if not global, at least a European investor base. But then when you come to the Swedish krona bonds that are issued mainly from Swedish companies which are in many cases unrated, I would say that the investor base is more Nordic, naturally in Sweden but also in other Nordic countries. And when you go to really small companies for example here in Sweden, and even in Finland, where there are smaller companies and smaller issuers and maybe better yields as well, then it's more local, the majority of the investor base is in the country where the bond is issued.

Tomas: So thanks to all these different characteristics, you actually get quite a nice yield pickup in many of the Nordic names and Nordic markets.

Jukka: Absolutely. And especially compared to European markets. Right now, the demand for corporate bonds is extremely high in Europe. When they bring a new issue, for example for a medium-sized company in the triple or double B area, books can be ten times oversubscribed and you have initially priced, let's say, 3%, and then the bond is at 2.5%, which is quite significant. For an equity investor or an equity analyst, it sounds like peanuts, but in the bond world, it's a giant, a very big difference.

Tomas: So Jukka, what would be the main things that an investor should have an eye on in this moment?

Jukka: What happens in the central bank world, that's kind of positive, and that the support for the markets continues. And the fiscal dominance: even the EU has managed and will manage the situation relatively well, the countries get the support that they need. Then it's pretty much a question of recovery – and recovery seems to be on its way.

Tomas: So Sauli, how is it in equities? What are the things that you are watching right now?

Sauli: Well, as Jukka said, we're all watching what central banks do as they are running the show at the moment, it has been for the past decade and will be for the next decade, I guess. Besides central banks and possibly inflation pick up, I think what we really need to focus on is the real economy and development of companies' earnings. What has happened during the Corona crisis is that the valuation levels have skyrocketed since the earnings have been kind of down here. So, in order for the equities to continue to perform, we need robust earnings growth. That's basically it, even though you can justify a higher valuation with the zero interest rates. Obviously, the current valuations, you cannot justify those, you need robust earnings growth. Basically, that's what I'm looking at. It's really during the upcoming quarters when the pandemic finally starts to fade out, we will see in what state our economy is and in what shape our companies are after the crisis. The outlook is good, I'm fairly optimistic but what I want to emphasize that without strong earnings growth the parties for equities cannot continue.

Tomas: How is it now during the first quarter and the ongoing reporting season? Has there been any big surprises, positive or negative?

Sauli: The currencies have gone well, the companies are in good shape they are performing well, considering the environment where the pandemic is still kind of dragging things down. The outlook for the current year is kind of - obviously, since nobody knows exactly when Corona will fade - it will weigh down the outlooks, companies are fairly

cautious with the outlooks. But overall, the earnings season has given a good start for the year and for the strong earnings growth expectations. They are definitely backing up their strong earnings growth expectations what we need here.

Tomas: We have discussed now for some time and we have touched on many of the issues that are making the Nordics so appealing for institutional investors. We have discussed how liquidity has evolved during the past year and we have talked about the outlook for this year.

So, in our next episode in April we will look back at Q1 for learnings before then moving on to the discussion of the ongoing AGM period and some governance issues. Joining me for that will be Evli's Head of Sustainability Outi Helenius and once again an expert from our partners.

Until then, please visit our Evli blog hub where you will find more information on the market outlook including an excellent Q&A with my colleagues Peter Lindahl, Janne Kujala and Ville Tiainen as well as our back catalogue of Evli podcast episodes. Now it just remains for me to thank my guests for today: Jukka Hyvönen, Evli's Sales Director in Stockholm and Sauli Vilén, Chief Equity Analyst at Inderes. Gentlemen, it has been a pleasure talking to you today.

Sauli: Thank you.

Jukka: Thank you, likewise.

Tomas: And thank you, dear listeners. Feel free to send us questions! The address is fundinfo@evli.com. I'm Tomas Hildebrandt and this is the Nordic Investor Podcast. Au revoir, auf Wiedersehen, bye bye.

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