Equity Research

Catella AB (CAT B)

Sweden | Financial Services | MCAP SEK 2906mn

22 February 2021

Buy

Target price:	46.9
Current price:	32.9
Upside	56.8%

Catella – Gold priced like dirt

Catella AB (CAT B) is a company operating within the real estate and funds segment in Europe. With a history of underperformance, it is now a company with proven and performing segments since it divested underperforming areas. The new Catella is estimated to grow AUM with a CAGR of 15.0% within the business area *Property Investment Management* (PIM) between the years 2020-2023. Due to the scalability of the business model in PIM, the EBIT margin is expected to grow from 22.1% to 30.6% during that time. Despite this strong growth and SEK 1.4bn in cash, the market is set on the past, valuing it at a 68.7% discount to peers. On a target EV/EBIT multiple of 8.0x for 2022E, a target price of 49.6 and an upside of 56.8% is justified for this misunderstood golden nugget.

Key takeaways

- **Strong continued growth in a highly scalable business** Property Investment management has grown its AUM from 31.6 SEKbn in 2015 to SEK 123.5bn in 2020E corresponding to a CAGR of 31.3% for the past 5 years. The segment is estimated to grow at a lower, though healthy, 15.0% CAGR until 2023 because of greater absolute numbers. The majority of costs are fixed, and an increase in AUM results in high EBIT conversion. As PIM is the largest business area, 72.4% of revenues and 91.0% of EBIT is expected to come from this growing segment in 2022. As a result, the net profit margin in the group is expected to increase from 10.5% in 2020 to 12.9% in 2022.
- **Divestment of underperforming business areas have left the company with a strong cash position** The divestment of Catella Bank in 2019 and mutual funds in 2020 has left the company with SEK 1454mn in cash. With 50.0% of market cap in cash, strong downside protection is given with an option in good returns. The cash can be used to boost investments in existing segments, for acquisitions, or to start development projects, with the goal of generating at least 20.0% IRR on these early-stage developments, where historical developments have exceeded that goal.
- **Sticky revenues in top ranked property funds** Typically, a lockup period of 2 years is applied upon investing in the funds, and an exit fee of 1.0% is applied upon exiting the fund, which incentivizes long term ownership. In turn, this creates steady revenue for Catella. In recent years, investors have been driven to the property market due to the low interest environment in Europe. In short, safe yield generating assets are in high demand from for example pension funds who need cash flows to meet payouts. Providing an easy option to invest in the asset class has proven to be a good niche with 31.3% CAGR in AUM since 2015. Until August 2020, 5 of the 16 most successful property funds YTD in Germany were run by Catella, which strengthens its attractiveness among investors.

Analyst	
Gustaf Bülow	Equity Analyst

Market Data, SEK	
Listing venue	Nasdaq Stockholm
Shares (mn)	88.3
MCAP (mn)	2906.6
EV (mn)	2863.6

Metrics & Drivers	20E	21E	22E
Curr. EV/EBIT	5.3x	6.1x	5.1x
P/E	11.7x	10.1x	7.9x
EPS	2.8	3.3	4.2
EBIT margin	22.8%	19.5%	19.8%

Forecast, SEKmn	20E	21E	22E
Total revenue	2357.3	2401.3	2842.2
Rev. growth y/y	-2.6%	1.9%	18.4%
EBIT	537.7	533.5	639.8
EBIT Margin	22.8%	19.5%	19.8%
Net profit	248.1	287.1	367.1
Net profit margin	10.5%	12.0%	12.9%

Major shareholders	
CA Fastigheter	47.5%
Avanza Pension	7.0%
Swedbank AB	4.3%
Total institutional	28.1%
Total insider	49.7%
Total	**77.8%**

Price Development, SEK

Investment thesis

Refinement to a performing real estate company.
Poorly performing segments within Catella have been divested, i.e the banking business, and what remains are segments that have proven themselves continuously with consistent profitability. The market seems to have missed the potential in PIM, a segment that has consistently provided profitable growth since reporting started in 2013. On top of that the company has its own development portfolio under principal investments, the latest project being sold in Q3 2020, generating SEK 170mn in profit, or 8.8% of market cap and an IRR of 36.2% exceeding the goal of 20.0% IRR. Today, there are four ongoing developments, The largest being Kaktus towers, expected to be sold in 2022, for a guided value of EUR 130mn.

Strong synergies and 2.1% market share provide a unique position for Catella.
While Corporate Finance is the segment with the lowest EBIT margin in the group (8.9% in 2019), it has a large contact network, a 2.1% market share in the European property transaction market in 2020, and vast knowledge in real estate transactions. This is not only an advantage to Corporate Finance itself, it also creates credibility for the entire group and strong advantages for PIM. Compared to peers, this is a unique feature for the company. While other peers have to outsource the acquisition and exit function of the business, especially within their property funds, Catella can use their in-house function for both acquisitions of real estate and when raising capital for new and old funds. These synergies create a unique and more effective company, and in turn it provides Catella with a strong market position for future growth throughout the European market.

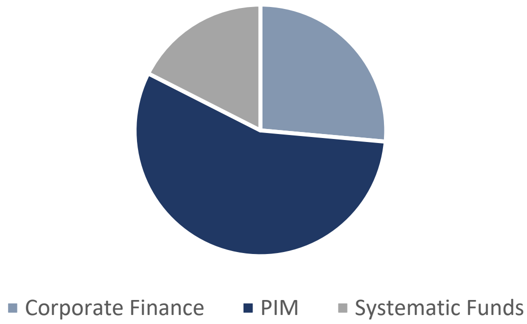
SEK 1454mn in cash acts as a defensive cushion and gives the company the ability to act opportunistically.
Due to the sale of several business areas Catella has been left with an extraordinary cash position (SEK 1454mn) compared to a market cap of SEK 2906mn. This cash can be used to fund further expansion or invest into the company's development projects, projects that have previously "far exceeded the company's goal of an IRR over 20.0%". Developments is something that the company will increase its focus on during 2021, and to increase transparency it will add the segment as its own business area in company reports. Because Catella is active in real estate, higher interest rates is something that concludes a risk to the business. Should bonds be more attractive to invest in, future growth in property funds and corporate finance will be affected. A worse environment in real estate does however provide opportunistic terrain for property asset management (PAM, part of PIM), which specializes in distressed assets.

Margin expansion from 12.1% to 24.9% within PIM.
After a long period of high levels of investments in PIM and 31.3% CAGR since 2015, AUM is now expected to grow at 15.0% but at higher profitability due to operational leverage because of a highly fixed cost structure. The investment mandates and fee structures within this segment generate sticky revenues and have remained attractive to investors due to their dividend profile and strong performance. Because of the downfall of the bond market, real estate is viewed as the next best option for investors who need steady streams of cash. Due to the scalability of the business net income margins are expected to grow from 10.5% 2020E to 12.9% in 2022E on a group level. In PIM, the EBIT margin is expected to grow from 12.1% in 2019 to 24.9% in 2022, this margin was unusually high at 29.1% this year due to the divestment of the development project, Grand Central.

Overview of the company

Traditionally Catella is associated with its funds and banking business, due to underperformance in these segments the company has now sold these and is now moving towards a pure real estate company. The company is now mainly active within the real estate segment in Europe and the UK through Corporate Finance, Property Investment Management and its Principal Investments. Catella is also active within the macrofunds segment because of its Systematic Macro fund, which trades sovereign debt, equity indices and currencies using a quantitative approach. 56.1% of revenue is generated within the PIM segment, followed by Corporate Finance, (26.4%) and Systematic Funds (17.5%).

Revenue split on estimates for 2020.



Source: Analyst estimates

Overview of the market

Naturally, business models differ between the three segments. Corporate Finance generates revenue based on the number and size of deals it takes upon. Systematic Funds invests money for institutional investors based on fundamental data it gathers and then analyzes using financial theory. PIM, the largest segment in the group, has two segments. Property funds is an asset manager which receives capital from institutional investors, and then allocates this capital according to the individual funds mandates. Property asset management acts as adviser to property owners on how to increase profitability and often in the exit process, where it generates exit fees. Most of the segment's assets consist of defensive assets, with 41.0% residential properties, 37.0% offices, 14.0% retail and 8.0% other, with the single largest exposure being Germany with 34.0%, followed by The UK and France at 18.0% and 15.0% respectively.

The European real estate market has been hit hard by the COVID-19 pandemic, especially retail facilities, it is however expected to make a cautious recovery in 2021 mainly due to large amounts of pent-up capital and future government programs in the UK[1]. Total market size was €566bn in 2019 with Germany, the UK followed by France being the biggest markets. The market is expected to grow at a rate of 0.7% on an annualized basis until 2024[2]. Underlying trends within the market include low interest rates, urbanization and an increase in the older population combined with declining capabilities from governments to house them in retirement homes.

1. https://www.pwc.com/gx/en/industries/financial-services/asset-management/emerging-trends-real-estate/europe-2021.html 2. https://www.statista.com/study/78757/real-estate-in-europe/

Financial forecast breakdown

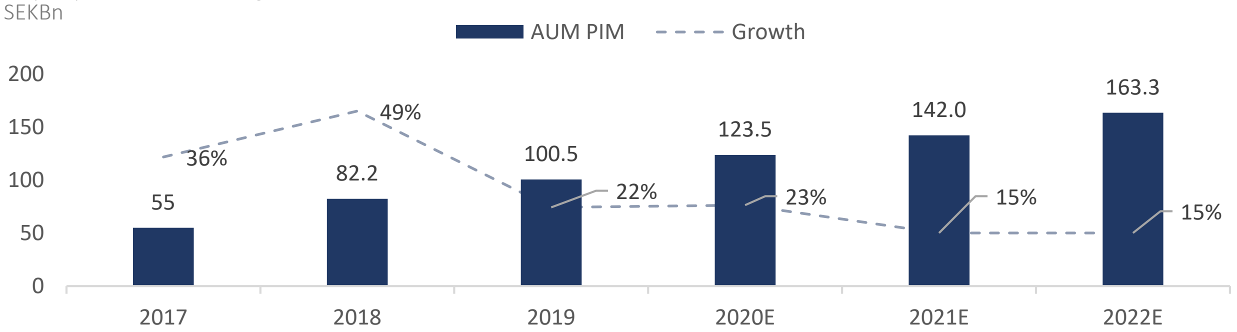
Revenue expected to increase to SEK 2842mn:
Due to differences in the business segments, revenues have been calculated separately in each business segment. On a group level revenue is expected to reach SEK 2842mn in 2022, a CAGR of 5.5% from 2019.

Corporate Finance has a high dependency on market sentiment:
Corporate Finances transaction volumes and in turn revenues, are highly dependent on the market outlook within Europe. The segment has historically held a market share of 2-3% within this market and is estimated to keep that share going forward. Given that the property transaction market is expected to make a full recovery in 2022, the Corporate Finance segment is estimated to keep a low EBIT margin due to highly fixed costs in the segment, from 4% in 2020 to 2% in 2022. Historically it has kept a fee of between 1.0 – 2.0% of transaction volumes. Until 2022 it is estimated to keep a 1.0% fee. In 2020 the fee has been 1.6%, however, its historical value is closer to 1.0%. The higher fee this year is expected to have been due to investors wanting deals closed faster. Due to the market operating largely the same way, a 1.0% fee is reasonable for the future. Which will create revenues of SEK 630mn in 2022, compared to SEK 623mn in 2020.

Weak performance in systematic funds:
Systematic funds is the smallest segment within the group and also the worst performing. While structural changes are being made, it is uncertain how these will affect revenues or how they will affect the cost base. AUM is expected to remain steady at SEK 19.3bn, and fees being 0.8% of AUM, revenue is expected to reach SEK 154mn in 2022. The segment is estimated to decrease staffing as a consequence of the restructuring, going from 66 employees in 2020 to 50 in 2022, which will decrease costs from SEK 391mn in 2020 to SEK 156mn in 2022, the large decrease being due to mutual funds being divested in Q3 2020.

Stable revenues in PIM:
Property funds is the largest part of PIM with 62.7% of revenues for the estimates of 2020. Investment mandates within the segment are long and generate stable revenues over time. Historically, PIM have generated fees of around 0.8-0.9% of AUM, with the variation being due to performance fees, generally around 20.0% over a certain hurdle rate. The fee is expected to remain between 1% in 2020 and 0.9% in 2022. These variations have occurred historically and they will occur again. Given a growth rate in AUM of 15% per year due to greater absolute numbers, revenues within the segment are expected to reach SEK 2057mn, 72.4% of the group total in 2022.

Property investment management AUM.



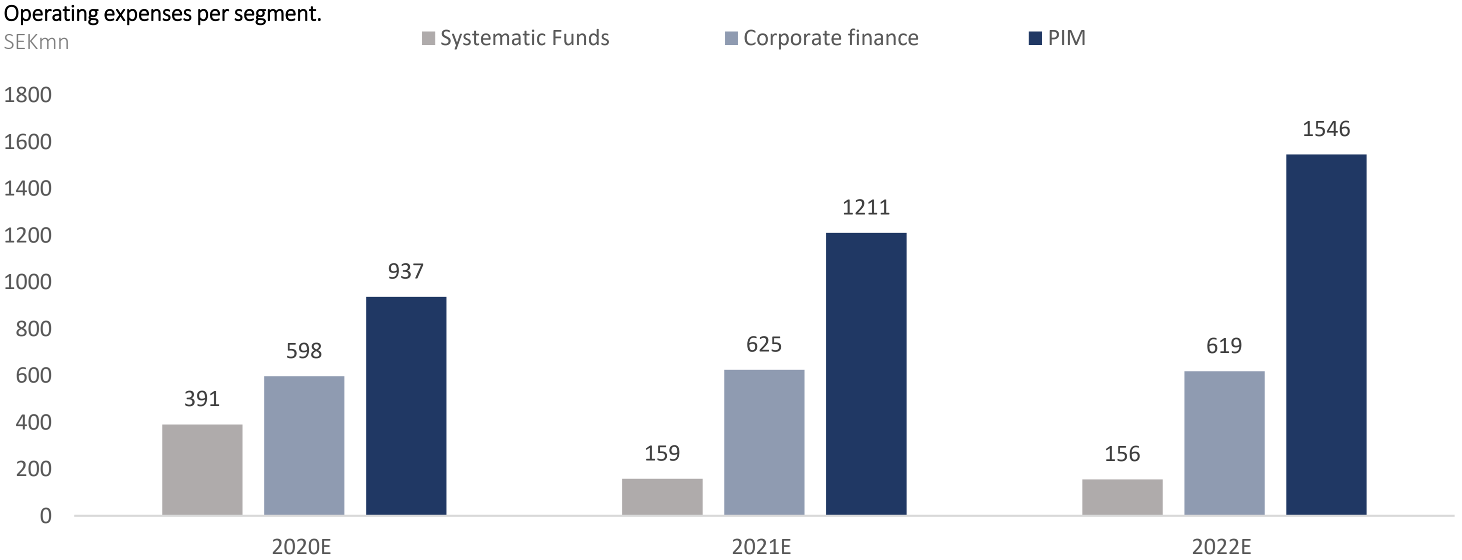
Source: Analyst estimates

Financial forecast breakdown

Increase in personnel and assignment costs will lead to an increase in operating expenses to SEK 2282mn:

On a group level operating costs are expected to increase from SEK 1819mn in 2020 to SEK 2282mn in 2022E. This is related to an increase in personnel costs from SEK 1473mn to SEK 1802mn on a group level and an increase of assignment costs. Employees are expected to increase during this period, from 489 in 2020 to 508 in 2022 due to further expansion in PIM. Assignment costs are costs related to a transaction, this could for example be research or closing costs related to a certain transaction, such as a new property or commissions in the FX market. When PIM purchases a new property for its funds, there are costs associated to each transaction, an increase in AUM means that new properties have to be purchased, Assignment costs are expected to increase from SEK 316mn in 2020 to SEK 448mn, with 78.7% of assignment costs expected to come from PIM in 2022. Corporate Finance is estimated to see a modest recovery of deal flow and as such will increase their costs from SEK 597mn to SEK 625mn due to an increased number of deals. On a group level the EBIT margin is set to increase from 2019 from 17.4% to 19.7% in 2022 due to the divestment of the banking business and scalability of PIM.

Operating expenses per segment.
SEKmn



Source: Analyst estimates

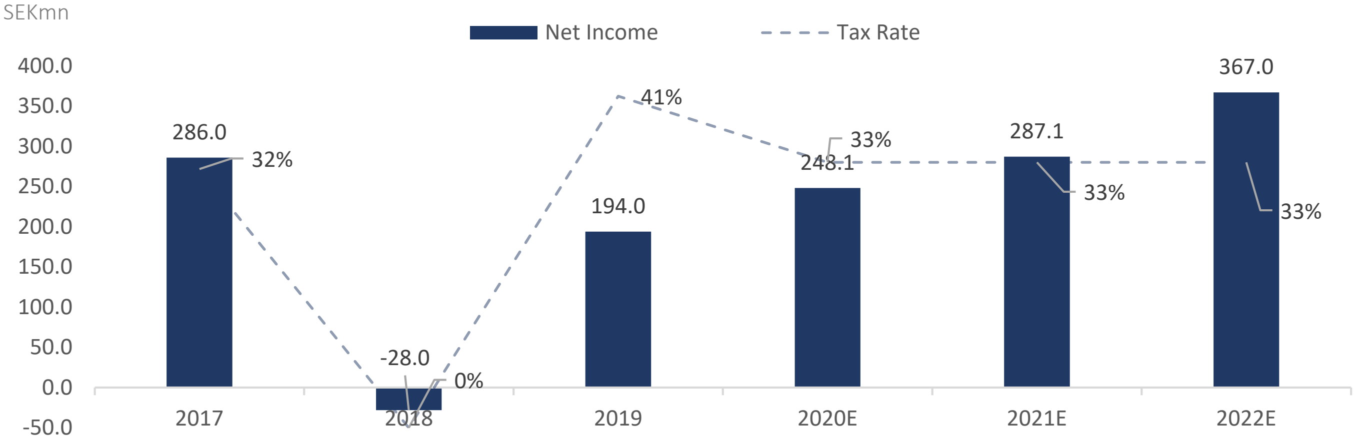
Steady amount of depreciation and amortization expected to be held at SEK 26mn:

A financial business such as Catella has a very low amount of capital expenses necessary to sustain its business, and as a consequence a low amount of depreciation of physical assets. In 2019 a large acquisition related amortization was made in intangible assets in IPM (Systematic Funds), APAM (UK Property asset management) and two small subsidiaries. This is to be seen as a one-off and Catella is expected to keep a low rate of depreciation at SEK 26mn.

Financial forecast breakdown

High tax rate expected to decrease from 38% to 32%:
Due to the divestment of first the card issuing business in 2017, and then the banking business in 2018 (ongoing), the company has remained in a constant situation of high tax rates. The reason for this is largely due to the fact that the company cannot carry costs related to the divestments. When the banking license is returned in the first half of 2021, taxes are expected to decrease rather quickly to a level of 32.0% in 2022E compared to 38.0% in 2020 which will boost net income. While these taxrates still might seem high, Catellas normalized taxrate is 27.0%, with the excess being due to limited contribution rights within the corporate structure. Interest expenses at SEK 20mn are mainly related to the outstanding bond loan, which matures in June 2022, Catella is expected to continue their borrowings which will leave interest expenses unchanged.

Decreased tax rate implies sharp increase in net profit.



Source: Analyst estimates

Income statement. SEKmn	2018A	2019A	2020E	2021E	2022E
Net sales	2159.0	2353.0	2357.3	2401.3	2842.2
Other income	57.0	67.0	0.0	0.0	0.0
Total revenue	**2216.0**	**2420.0**	**2357.3**	**2401.3**	**2842.2**
Direct assignment costs + comission	-389.0	-372.0	-315.8	-340.1	-448.2
Operating expenses	-1449.0	-1498.0	-1477.8	-1566.6	-1808.2
EBITDA	**378.0**	**550.0**	**563.7**	**494.5**	**585.8**
Depreciation and Amortization	-26	-128	-26	-26	-26
EBIT	352	422	537.7	468.5	559.8
EBIT margin %	16%	17%	23%	20%	20%
Financial items	-15	-138	-20	-20	-20
Taxes	-127	-135	-179.6	-161.5	-172.7
Net income	**210.0**	**149.0**	**338.1**	**287.1**	**367.0**
Income from divestments held for sale	-238	45	-90	0	0
Net profit	**-28.0**	**194.0**	**248.1**	**287.1**	**367.0**
Net profit margin %	-1.3%	8.0%	10.5%	12.0%	12.9%

Valuation

Better company, lower valuation.

The market has missed recent changes and is valuing Catella lower than its 5-year historical average of 5.5x EV/EBIT, despite better growth prospects and future margin expansion. Valuing it at just the historical multiple would indicate an upside of 3.7%, however, the business today is largely different than what it was 5 years ago. The "new" company has a higher EBIT margin at 22.8% in 2020 compared to 13.9% in 2015 and better prospects for growth. Based on the fact that the company has an enormous cash position and low debt financing, using an EV/EBIT multiple is best fit to value the company. Given that Catella has a lower EBIT margin than peers, largely due to lower margins in both the corporate finance and systematic funds segments, it should not trade at comparable multiples. On a target EV/EBIT multiple of 8.0x on 2022 estimates, the fair value of the company is 49.6 SEK indicating an upside of 56.8%.

Peer table		EV/EBIT	P/E	EBIT margin
Company name	MCAP SEKmn	2022E	2022E	2022E
EQT	243489.1	32.1	35.0	60.0%
Capman Oyj	4205.1	12.3	12.0	57.6%
Patrizia AG	22101.82	17.0	19.1	36.0%
Eq Oyj	7312.7	15.7	20.3	55.0%
Median	**14707.2**	**16.3**	**19.7**	**56.3%**
Catella	2906.6	5.1	7.9	19.7%

Peer valuation method implies high upside.

Using a peer-valuation method, compared to the median EV/EBIT multiple of 16.3x based on estimates for 2022, Catella trades at a significant discount, indicating an upside of 219%. Catellas closest listed peer, Patrizia AG, trades at an EV/EBIT multiple of 26.1 for 2020 and a price earnings multiple of 30.6, compared to Catellas multiples of 5.3 and 11.7 respectively. Remaining peers also trade at a large premium to Catella, these businesses all have private equity segments which boost their EBIT margin and makes them less comparable than Patrizia.

Unreasonably discounted cash position.

The company's cash position is not something that should be underestimated when valuing the company. In the future, the company is estimated to use this cash to fund future acquisitions and invest in future development projects, projects that have exceed 20% IRR historically. While the market seems to be skeptical regarding the company's ability to make sound acquisitions, perhaps due to the failed acquisition of IPM (Systematic Funds) in 2017, Its most recent acquisition of APAM in 2018 has provided the company with geographical breadth within property asset management and further synergies with property funds. When considering that Systematic Funds was an acquisition made in the "old" business, the market should not discount the cash as it is doing now. Because the company themselves are very secretive regarding what the cash will be used for, it is best thought of as a proper margin of safety with an option in value creation.

Because the company has a 65.0% lower EBIT margin than the median of peers on the estimates for 2022 but has better growth prospects than the closest peer Patrizia, an EV/EBIT multiple of 8.0x is justified. This is not only is closer to its historical average and peers, it also takes into account future growth prospects. Note that this is still at a discount of 49.0% to peers.

Management and board

Johan Claesson, acting CEO and member of the board:
Johan Claesson has previous experience mainly within his family company Claesson and Anderzén, which is also the largest owner of Catella, and companies within the sphere.

Ownership (private and through companies): 1 100 910 Class A shares and 42 563 838 Class B shares or 47.5% of the company.

Christoffer Abramson, CFO:
Christoffer Abramson, CFO: Christoffer has previously been CFO of EF real estate holdings in Boston and at GE real estate in London. He holds a masters degree of economics from Stockholm School of Economics.

Ownership: None. Incentive scheme of 250 000 options series A and 250 000 series B. Exercisable 2024 and 2025 respectively.

Jan Roxendal,acting chairman of the board:
Jan Roxendal has previously worked as the CEO of Gambro and Intrum Justitia. He is currently the chairman of the Swedish pension fund, AP2 and member of the board in Magnolia bostad.

Ownership: 129 544 Class B shares or 0.14% of the company. SEK 2mn in bonds.

Joachim Gahm, member of the board:
Joachim Gahm is currently the chairman of Arise AB, Sustainable Growth Capital and a director of Kungsleden AB. He has previously served as president of Öhman Investment AB.

Ownership: None.

Appendix

Company: Catella AB	Historicals				Estimates			
SEKmn	2016	2017	2018	2019	2020E	2021E	2022E	2023E
Net sales	2007.0	2461.0	2159.0	2353.0	2357.3	2401.3	2842.2	2688.4
Other operating income	20.0	16.0	57.0	67.0	0.0	0.0	0.0	0.0
Revenues	**2027.0**	**2477.0**	**2216.0**	**2420.0**	**2357.3**	**2401.3**	**2842.2**	**2688.4**
Direct assignment costs and comission	-417.0	-479.0	-389	-372.0	-315.8	-340.1	-448.2	-374.5
Other external expenses (2020-2023 includes personnel)	-441.0	-496.0	-471	-451.0	-1473.8	-1561.6	-1802.2	-1617.9
Personnel costs	-878.0	-1030.0	-960	-1043.0				
Depreciation and amortization	-14.0	-28.0	-26	-128.0	-26.0	-26.0	-26.0	-26.0
Other operating expenses	-14.0	-29.0	-18	-4.0	-4.0	-5.0	-6.0	-7.0
Amortization of acquisition related intangible assets	-4							
Items affecting comparability		-53						
Operating profit/loss (EBIT)	**259.0**	**362.0**	**352.0**	**422.0**	**537.7**	**468.5**	**559.8**	**663.1**
EBIT margin %	*12.8%*	*14.6%*	*15.9%*	*17.4%*	*22.8%*	*19.5%*	*19.7%*	*24.7%*
Interest income according to effective interest method	24.0	23.0	2.0	2.0	0.0	0.0	0.0	0.0
Interest income other			16.0	12.0	0.0	0.0	0.0	0.0
Interest expenses	-11.0	-17	-27.0	-49.0	-20.0	-20.0	-20.0	-20.0
Other financial income	260.0	41	30.0	15.0	0.0	0.0	0.0	0.0
Other financial expenses	-34.0	-12	-36.0	-118.0				
Financial items -net	239.0	35	-15.0	-138.0	-20.0	-20.0	-20.0	-20.0
Profit/loss before tax	**498.0**	**397.0**	**337.0**	**284.0**	**517.7**	**448.5**	**539.8**	**643.1**
Tax	-141.0	-111.0	-127.0	-135.0	-179.6	-161.5	-172.7	-192.9
Net profit for the year			210.0	149.0	338.1	287.1	367.0	450.2
Operations held for sale:								
Net profit/loss for the year from divestments held for sale	0.0	0.0	-238.0	45.0	-90,0	0,0	0,0	0,0
Net Profit for the year	**357.0**	**286.0**	**-28.0**	**194.0**	**248.1**	**287.1**	**367.0**	**450.2**
Net Profit Margin %	*17.6%*	*11.5%*	*-1.3%*	*8.0%*	*10.5%*	*12.0%*	*12.9%*	*16.7%*
Profit/loss attributable to:								
Shareholders of the Parent company	272.0	192.0	-112.0	113.0	166.2	192.3	245.9	301.6
Non-controlling interests	85.0	92.0	84.0	80.0	81.9	94.7	121.1	148.6
Sum	**357.0**	**284.0**	**-28.0**	**193.0**	**248.1**	**287.1**	**367.0**	**450.2**

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