June 28, 2009
VOL 26 NO 26

www.tribune.ie
TribuneBusiness

Stockholm syndrome: although Irish problems are of a much greater scale, Brian Lenihan will be hoping Nama can replicate Swedish success

Eyeing up the successful Swedish model

Sweden did something similar to Nama before, through a company called Securum. Based on research of that example, Bill Nowlan outlines the challenges that lie ahead

NAMA is being assembled on its launch pad for its journey to save the Irish banks and the economy. We wish it well on its journey into the unknown. It is a journey that needs to succeed and do so quickly so that the property industry and the country can get back to normality as soon as possible.

Nama will be the biggest property 'show in town' and will impact hugely on investors, professionals, builders and many others, including the taxpayers. In an attempt to take a long view of Nama's likely journey over the next five to 10 years, I have researched several academic studies on the Swedish experience of 'Securum AB', their equivalent to Nama which operated in the early to mid-1990s. I have used information from a study by the Stockholm School of Economics of 2003 (by Clas Bergstrom, Peter Englund and Per Thorell) and a report by Danske Bank of 2008.

The Swedish banking crisis of the early 1990s has remarkable similarities to what has recently happened in Ireland. In Sweden, the first visible signs of crisis came in autumn 1990 when banks who lent money to commercial real estate investors began having problems finding buyers for their debt. The Swedish Treasury gave credit guarantees to assist those banks to raise funds. But this did not work and the crisis cascaded to include the major Swedish banks. During 1992, Swedish property prices declined rapidly, producing credit losses on the banks balance sheets. Simultaneously, the Swedish economy went into recession.

In January 1993, Securum, the Swedish equivalent of Nama, was set up and quickly became the owner of its first tranche of assets, comprising about 2,500 commercial properties with an estimated market value of 15bn-20bn Swedish kroner (€2bn-€2.5bn).

The tricky issue for Securum and its state shareholders was – as it is now for Nama and the Irish government – how to value the debt and the collateral being transferred. If the value of this debt was set too low, the banks would go bust and require state support; if it was set too high, the taxpayer would risk making a bad deal. The guiding principle decided upon was to make conservative estimates rather than optimistic ones. The Swedish state created a valuation board made up of experts on real-estate assessment in order to double-check the valuations made by the banks themselves before transferring to Securum. I will return to this topic shortly.

Securum started out with a massive portfolio of loans in default. The number of borrowers on its client register was about 1,000. By the middle of 1994, just 18 months after it was established, 70% of the 800 limited companies were declared bankrupt or liquidated.

After the loan-liquidation phase, efforts focused on measures aimed at generating value in the assets, and selling properties at the best possible price as soon as possible. Most of the sales took place in 1995-96 when the Swedish and international property market had stabilised.

Securum used three methods of disposal: individual properties sold one at a time; groups were lumped together into bigger packages; and property companies were sold. However, the larger sales of properties occurred by selling off whole property companies. Securum decided not to go the auction route – as had been used by the RTC in the US during their banking crisis in the mid 1980s – as "the circle of potential buyers in Sweden was limited and this might open the door for collaboration between buyers aimed at keeping prices down".

In fact, Securum chose to sell individual properties and packages of properties following direct negotiation with selected potential buyers. It also created five stock exchange-listed property companies through IPOs.

It is unclear how long the state planned to keep Securum in operation. The idea was that it should be possible to continue operations for up to 15 years. However, three years after its creation, the ministry of finance indicated that five years "ought to be perfectly sufficient for winding up Securum's portfolio of loans". Securum was eventually wound up by mid-1997.

As to the effect of the whole project on taxpayers, the total investment by the state was SKR71bn (€9bn) and the proceeds from asset sales and dividends etc amounted to SKR36bn making a total cost to the state of SKR35bn (or about €4.5bn). This, in cold terms, was a haircut to the Swedish taxpayer of about 50% of the funds advanced. As to the success of Securum, there is wide consensus that the project was a success and that the opportunity cost of not having dealt with the crisis would have been significantly higher.

So what would my comment be in the light of this Swedish experience?

Firstly, the size of the Irish problem is a multiple of the Swedish one. Nama will have a loan book with a cost of about €50bn-€60bn, equating to 27%-33% of Irish GDP, whereas the Swedish equivalent was less than 3% of its GDP. This much larger portfolio will affect both the timescale and the impact of the operation on the Irish market. Ireland will effectively have one main supplier of development land and buildings for a long time unless Nama moves quickly and deliberately to stimulate the market by parcelling their assets out to new owners – possibly in bulk.

Secondly, the Swedish experience was not pain-free to the taxpayer who took a 50% write-off of the state's investment. Is Nama likely to do better with its €50bn-€60bn?

Thirdly, Sweden was not a member of the EU in 1992. The EU has written to all member governments declaring that if the valuations of the assets subsumed into Nama are not fair, that any overpayment to a bank for its portfolio will be regarded as state support. Also, the EU is attempting to draw a distinction between the traditional and internationally endorsed 'Mark to Market' approach to valuation with a new approach called 'Economic Valuation'. This will create considerable problems for Nama as they will probably be the first institution to encounter this challenge.

Bill Nowlan is a consultant property asset manager with WK Nowlan