

# A Swedish look at PE in Norway: Interview with Bengt Hellström – Head of alternative investments in the Swedish AP3 fund

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In a small country like Norway, domestic investors often get biased by their close proximity to local finance and business. Domestic investors differ from foreign investors who operate with an arm's length relationship to local fund managers, investment cases and the local business climate.

At the same time, large foreign investors are often stronger when it comes to comparing the strengths and weaknesses of different markets. Lately, the Swedish investment director Bengt Hellström has gathered extensive experience from investing in PE funds in Norway, as well as other countries. He aroused our curiosity. Why did he choose to place a disproportionately large share of AP3's private equity investments in Norway? Is it due to an attractive potential investment universe, is it due to strong fund managers, or is it basically coincidence? After all, the Norwegian PE market is young and quite small.

I took an early Monday morning flight to Stockholm to meet him on his home ground. The AP3-fund office is by not at all a flashy place. It radiates modesty and seriousness and is located respectably far away from the financial cluster in Stockholm. This comes as no surprise. The AP3 fund serves as a state-owned buffer fund for the Swedish public pension system. So there is no need to attract investors or clients through a fancy and rich image. Today, the fund manages approximately EUR 25bn, out of which EUR 1.7bn is allocated to PE, predominantly placed in Western Europe and the US. Bengt and his team rarely invest more than EUR 30mill in a PE fund and never less than EUR 15mill. In other words, the range of exposure to one single fund is rather narrow, implying that involvement in small venture funds is fairly limited.

In Sweden, the fund is one of the largest institutional PE investors. It is well known for its position among Nordic players. To have the AP3 name on the LP-list is by all standards a quality sign for Nordic PE funds. In addition, Mr Hellström has found it challenging and enlightening to help relatively young PE funds in dealing with international investors and expanding into new markets. Several Norwegian PE funds have enjoyed his experience relating to LP/GP contracts and agreements.

In Norway, the AP3-fund has committed close to EUR 130mill in the funds Ferd Private Equity I and II, Hitec Vision IV, Neomed Innovation IV and Verdane Capital IV, IV Twin, V and VI. So a substantial share of their alternative investments is tied to Norwegian PE funds.

In comparison, investments in Finland are limited to the Capman funds, while AP3 has no investments in Danish PE funds.

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But why devote this much attention to the Norwegian PE market? In size, the market is not that much different from the Finnish and the Danish. In addition, several financial players point to an industry structure where performance is highly sensitive to variations in oil and raw material prices as well as the business cycle in general.

– It is true that PE investors favour more traditional manufacturing sectors where it is easier to develop a sound value enhancement plan, remarks Hellström. I think it's a fact that investment managers, both among the LPs and the PE fund managers, tend to favour the sectors that they know the best. This may affect the investment pattern. Having said that, the petroleum-related investment cases in Norway are not predominantly related to pure oil extraction. Many of them sort under oil services, which are less sensitive to variations in oil prices. Through Norwegian PE funds, we have also invested in salmon

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breeding companies. At the time of investment, they were not viewed as much of value, but apparently we were lucky, as the market for salmon improved markedly over the following years. The Norwegian shipping industry is potentially the one industry that is most strongly ridden by booms and busts. The competency of PE investors and a leveraging strategy does not fit into such a pattern.

What about retail trade? There is not much PE investment in that sector in Norway.

– My impression is that just like in Sweden and many other small countries, retail trade is dominated by many small local players. In that respect, there is possibly a potential for value enhancement through national consolidation.

But in Sweden you have large international success stores like H&M and IKEA. Is there something about the Swedish market that makes it more attractive as a platform for international expansion?

– Actually, the number of Swedish retail stores with widespread international success like H&M and IKEA, is quite small. There are a lot of Swedish chain stores that do well in the Nordic market, but they really struggle to take the big step and be successful in the larger markets. Lindex, Stadium, KappAhl are typical examples of this pattern. Norway is probably equally well suited for Nordic or international expansion in the retail trade segment. I don't really see the difference between Norway and Sweden in that respect.

So what is your impression of the future investment potential through private equity?

– In the short term we may face a period of dampened activity, but in the long term I see a broad potential for alternative investments through PE funds. When it comes to the Nordic market, I think the potential for profitable investments in Norway is large. In Sweden, the PE market is probably more saturated with capital.

Do you believe foreign investors will become more interested in the Norwegian market?

– Probably, but international investors need more information on Norwegian funds and the potential investment opportunities in order to increase the interest.

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I think that a Nordic base for a PE fund provide a large advantage, but such a strategy requires the establishment of local teams in all the countries where you operate. Geographical distance is no advantage for a PE investor. Traditionally, few Norwegian funds have operated with a clear Nordic investment strategy. In the venture segment I believe that Northzone is the only company with such a strategy. In the expansion and buyout segments the number is clearly increasing.

Are you satisfied with returns on PE investments in Norway?

– Yes we are. So far we have experienced an overall annual rate of return close to 19% on our investments. Some of the funds, among those some of our Norwegian investments, have really over-performed. But we are more realistic in our long-term expectations. Our objective is to reach an average annual return of 15% over a 3-year period. Considering that the PE industry in Norway is relatively young, I am more than satisfied with the level of competency and professionalism among GPs and investment managers.

Speaking of returns, why do you think buyout investments generate higher returns than more early-stage investments in Europe, while it's the other way around in the US? Is the buyout market in the US over-crowded?

– No, I think there is a different story behind this pattern. The venture capital market in the US is significantly more developed. It has a history going back more than 30 years. When you cross the Atlantic and meet representatives from the VC industry, you are struck by the size of the industry, the role it plays in the US and the level of development. In time, I believe we will see an improvement in European VC returns as this market becomes more mature.

Whats your opinion on how the VC and PE business dealt with the widespread critique last year regarding transparency and ethics?

– I believe the debates last year was a real wake-up call for the industry. The strong focus on this subject during the World Economic Forum meeting is a clear sign of

industry representatives taking serious action to meet the concerns expressed. Still I think the industry has a lot of potential when it comes to improving transparency and handling of information. In Sweden, the venture capital association is now working intensively on these matters. In my daily work I do not experience such a strong scepticism towards this asset class. In our dialogs with for instance the Swedish LO, we have only received positive feedback on our involvement in PE. Our own investment standards expect that PE funds receiving investments from AP3 fulfils all ethical and tax related requirements. The tax matter has received some attention in the Swedish debate.

Bengt Hellström spent 6 years as a partner in EQT, one of the largest and most successful PE houses in Sweden, before assuming the responsibility for managing alternative investments at AP3. Based on this experience I wanted to test his response to a slightly more controversial question. Why are there so few women among partners and top investment managers in the Nordic VC and PE management companies? In my opinion, the gender pattern is even more skewed than among stockbrokers and equity analysts. After all, we live in the Nordic region where women participate actively in most sectors of the economy.

– I think it's a complicated question, but the main problem probably relates to the career moves among people in their late twenties. In PE management companies, people usually start their career at this point, some years after finishing education. This is exactly when most women don't work continuously for 5-10 years. Unfortunately, I think this industry is especially sensitive to these choices. This since, successful investment teams often require stability among members over a long time period. This may also contribute to explain the biased gender pattern in the industry. ■

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