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Continuous improvement creates value

A distinguishing quality of successful companies is their ability to continuously improve their operations and strengthen their market positions. It is a matter of adapting to new conditions, but just as much about strengthening the offering and increasing competitiveness.

As a long-term investor and engaged owner, Industrivärden therefore puts great emphasis on ensuring that its portfolio companies continuously develop their businesses and strengthen their capacities with a distinct focus on value creation. As a long-term asset manager, we encounter the same challenges in our own work on generating a competitive return. It is therefore important that we continuously improve our asset management model in order to capitalize on our full potential.

Since taking office as CEO nearly a half-year ago I have dedicated myself primarily to learning more about Industrivärden and our investments. A great deal of time has also been spent on the review of Industrivärden's strategy. This work has been conducted in close dialog with Industrivärden's board of directors. I have also benefited greatly from all of the meetings I have had with shareholders, co-investors and other key stakeholder groups as well as with my new colleagues. A couple of important insights that I have gained from this review are that there are no direct synergies between the portfolio companies, and that every investment must be evaluated on its own merits. It is also important that we increase our room to maneuver by achieving a lower level of debt over time. Last, but not least, Industrivärden should have a dividend policy that ensures a positive cash flow and gives us flexibility to adapt to external circumstances.

Based on my analysis of the operations and on my previous, professional experience, I can say that Industrivärden stands on firm ground. We have substantial knowledge and experience as an owner, a long-term asset management perspective, strong positions of influence, and investments with good value potential. At the same time, there are areas in need of development. Industrivärden's overall strategy – to be a long-term, value-creating asset manager through active ownership in Nordic companies – remains firm. Within this strategy we are now taking a number of

important steps to strengthen our ability to create shareholder value. Some are more concrete measures, while others entail a changed approach that will bear effect over time. In short, it is a matter of bringing about an accelerated pace of change and having less patience with low-performing investments.

A stronger Industrivärden

These steps are summarized in the following points:

- ***We are sharpening our focus on returns and clarifying our active ownership***

Industrivärden invests with a long-term perspective. This is a natural consequence of the fact that we have chosen an asset management strategy that builds upon involvement through active ownership. Long-termism is a strength that enables us to support short-term, difficult development steps that can generate high returns over time. At the same time, it is a challenge to know when to exit or reduce a holding in favor of another alternative. We are now sharpening our focus on returns, which will likely affect the pace of change in the portfolio over time.

As an active owner with substantial shareholdings, we can influence our investments. It is therefore important that we become clearer in exercising our ownership role. One way we are doing this is by strengthening our involvement in nominating committees. Industrivärden is to be represented by individuals from the Company's board or management. I personally have the benefit of participating in this important work as chair of the nominating committees of Handelsbanken, SCA, Skanska and SSAB. Through this work we are continuously broadening our network with talented individuals who we can nominate for board election. This is having an impact already during the current board nomination season.

We will also work in various ways to bring about a faster pace of change in companies facing substantial challenges. The appointments of new CEOs at Sandvik and Volvo are good examples of important changes that we support in our role as an engaged owner. Finally, steps have been taken to strengthen Industrivärden's

governance structure, among other things by preventing so-called personal constellations.

- **We are strengthening our relationships with other owners and various capital market actors**

By developing our relationships and cooperation with other owners and important actors, we can increase our influence. We will be a responsive and professional investor that is perceived as being an attractive business partner. This must permeate the entire organization, and for my own part, I have already met a large number of representatives in the areas I mentioned above, and this work continues.

- **We are broadening our investment universe**

Industrivärden will continue to invest in listed Nordic companies with good return potential. Our active ownership will build upon a foundation of trust and ownership-based influence. Our share of ownership should therefore be at least 10% of the votes. We are now broadening our investment universe by also looking at slightly smaller companies. For new investments, a candidate should have a minimum market cap of roughly SEK 3 billion. If we invest in a company with a market cap of SEK 3–10 billion, a 20%–30% equity stake is desirable. The idea is to have a genuine position of influence and that the investment's potential return will make a tangible contribution to the equities portfolio as a whole.

Active owners play an important role in society

To create long-term favorable returns for our shareholders, we must be a responsible and appreciated owner that looks after the portfolio companies' long-term development. We do this best by helping to build companies that continuously develop and strengthen their competitiveness in increasingly global and competitive markets. Like our portfolio companies, we are part of the environment we work in and must always strive to be a good force in society that contributes to sustainable development through our operations. This also benefits the communities that the companies work in. Our overarching approach in society is described in the Code of Conduct that was adopted by the Board in 2015.

Modest growth with large regional differences

Global rate of growth slowed in 2015, but remained on par with a year earlier and the IMF's forecast for 2016–2017. From a five-year perspective, the rate of growth has slowed steadily in emerging countries, while it bottomed in 2012 for the world's developed economies. During the second half of 2015 and start of 2016, uncertainty has risen, and there is a risk that the year's forecasts will be adjusted downward. Key causes are falling commodity prices, continued low productivity growth, and major exchange rate movements resulting from regional imbalances and geopolitical tensions. This includes China, but also several Latin American economies, which are also being weighed down by political uncertainty. It is positive to note, however,

that the slow recoveries of developed economies – the U.S. and Europe – appear to be continuing.

From a broader perspective, demographic changes, low productivity growth and high debt point to low growth, low inflation, and low interest rates for a long time to come. For Industrivärden's portfolio companies this requires continued adaptation to the prevailing market conditions and strong focus on efficiency and costs. At the same time, it is important to work with a longer perspective and create favorable conditions for profitable growth initiatives over time.

Relatively good growth in value in 2015

Despite the uncertain outlook, the stock market continued to perform well, and in 2015 the Stockholm Stock Exchange gained 7%, after reaching a peak of 19% in April. Performance of the equities portfolio was mixed, with SCA generating a solid total return of nearly 50%. For other portfolio companies the total return was below the market, and SSAB showed a clear negative return. From a three-year perspective, ICA Gruppen and SCA have clearly outperformed, while Volvo, Sandvik and SSAB have performed considerably worse than the market. Other companies have generated returns that are level with the market's return index.

During the year, net asset value grew by SEK 0.7 billion to SEK 69.1 billion, or 5% including reinvested dividend, compared with 10% for the total return index. The total return was 15% for the Class A shares and 11% for the Class C shares. The considerably higher growth in the share price during the year than growth in net asset value points to a sharp narrowing in the discount to net asset value during the year. During 2015 stocks were sold for SEK 1.9 billion, net. The single largest stock sale was in Kone, where the entire holding was sold for SEK 1.2 billion.

Investments with favorable return potential

During 2015 our portfolio companies had mixed performance. Handelsbanken, SCA, Ericsson, ICA Gruppen and Skanska showed favorable, stable performance, while Sandvik and Volvo are undergoing major, strategic change processes. Following its merger with Ruukki, SSAB is developing in the right direction, but is affected by very difficult market conditions.

Handelsbanken continues to perform well and is growing organically primarily in the UK. Like other banks, its business is adapting to changed regulations and digitalization in society. During the year Frank Vang-Jensen took office as new CEO, and Pär Boman was elected as new Chairman of the Board.

SCA is performing very well both operationally and in terms of value. Over several years the company has focused its business, carried out a number of product portfolio changes, and strengthened its positions in its core businesses, hygiene and forest products. A split into two divisions is therefore a natural step in SCA's ongoing development. In 2015 Magnus Groth took office as new CEO, and Pär Boman was elected as new Chairman of the Board.

The *Volvo Group* is currently in a process of change and is facing major challenges. This work is being led by CEO Martin Lundstedt, who newly took office and has many years of experience from the heavy automotive industry. An extensive process is now being carried out to simplify the company's structure, increase profitability and strengthen its presence in key growth markets. Volvo has overall strong market positions and favorable conditions to develop well over time.

Significant management changes were also carried out at *Sandvik* in 2015. Johan Molin was elected as new Chairman of the Board, and Björn Rosengren took office as new CEO. The company has been carrying out a transformation process for the past couple of years, but a number of important steps remain before Sandvik will be able to realize its full potential. With a foundation in the company's exceptional products, dedicated employees and strong brand, I feel that Sandvik has good prospects for future value creation.

Ericsson is showing an impressive ability to adapt and build strong positions in a rapidly changing industry with continuously shifting technology. Ericsson's strategic partnership with the IP company Cisco is a good example. At the same time, Ericsson must gain a better financial outcome from its positions of strength and increase profitability in several areas of its business.

During 2015 *ICA Gruppen* made several important structural deals, including the divestment of ICA Norway and the acquisition of Apotek Hjärtat. The company has an impressive market position and is showing favorable, stable performance.

Skanska continued to deliver growth in its profitable construction business and value-creating project development business. At the end of 2015 a new, strategic plan was presented for the coming five years. Skanska's business plan and financial targets have been updated, but its strategic direction remains firm. The company's nominating committee has proposed Hans Biörck for election as Chairman of the Board ahead of the 2016 Annual General Meeting.

For *SSAB*, 2015 largely involved creating continued synergies following its merger with Ruukki as well as improving the efficiency of operations and adapting to the difficult market situation. At its 2015 Annual General Meeting, Bengt Kjell was elected as the new Chairman of the Board.

Strong position for competitive returns over time

Industrivärden is in a favorable position to conduct successful, long-term asset management based on active ownership. Starting from our strengths, a professional organization and the development steps we are now taking, I look forward to leading the business to generate competitive shareholder value over time.

Stockholm, February 2016

Helena Stjernholm
CEO

