



CEO's message

2016 – A STRONG YEAR FOR INDUSTRIVÄRDEN

During 2016 our net asset value increased by SEK 13.7 billion to SEK 82.8 billion, and taking into account reinvested dividend, growth in net asset value was 23%. The total return for the Class A and C shares was 17% and 21%, respectively, and exceeded the Stockholm Stock Exchange's return index by a full 7 and 11 percentage points, respectively. This performance reflects a good year for the stock market, but also generally good growth in value for our portfolio companies. This applies in particular to the portfolio companies that have taken major change measures designed to boost profitability and capital efficiency. The largest growth in value was in Sandvik, where our holding grew by SEK 5.7 billion, or 52%. Volvo was a good number two, with growth in value of SEK 3.7 billion, or 32%. If we raise our sights a bit and look at the value potential a bit more long-term, we can see a number of important activities that were carried out during the past year for future value creation. Among other things I am referring to the announced split of SCA into two companies and SSAB's rights issue. Last, but not least, at Industrivärden we have conducted extensive development work within the framework of the refined strategy that was presented in February 2016. The aim is to utilize our full potential and further strengthen our ability to create shareholder value. This is an ongoing process, but allow me to briefly describe what we have done during the past year.

REFINED STRATEGY THAT HAS GENERATED TANGIBLE RESULTS

Our aim is to be a professional asset manager with the flexibility to act when opportunities arise. This ambition is expressed in, among other things, a new debt policy

and a new dividend policy. To ensure financial flexibility, the debt-equities ratio should normally be in the range of 0%–10%. During the year we carried out a number of transactions in our long-term holdings which, together with the growth in the value of our equities portfolio, helped lower our debt-equities ratio by just over 3 percentage points, to 12% at year-end 2016. We will continue to reduce our debt-equities ratio when the occasion rises in order to increase our financial flexibility to act over time. Industrivärden's convertible bond of EUR 550 M matures on February 27, 2017. The time period during which convertible owners could request conversion has passed, and approximately 9% of the convertible bond, corresponding to EUR 50.9 M, will be converted to new shares. The total number of shares will increase by just under 0.7% with the issue of slightly more than 2.8 million new shares. The remainder of the loan will be replaced with more flexible financing within the framework of our debt portfolio. To build up investment capacity, a positive cash flow is needed before portfolio changes and after paid dividends. In 2016 cash flow before portfolio changes amounted to approximately SEK 700 M, and the dividend that has now been proposed by the Board in 2017 enables a continued positive cash flow. Against the background of the Board's adoption of the aforementioned policies, Standard & Poor's raised Industrivärden's credit rating to A/Stable/A-1 in 2016.

Industrivärden's asset management model – active ownership – draws from our strengths in the form of influence, knowledge, a strong network, owner collaboration, financial strength and genuine involvement. From this model it follows that we work with a long-term perspective when we evaluate our investments. This in itself is a strength that enables decisions that benefit the portfolio companies' value growth over time. At the same time it is imperative that we act as a financially rational asset manager when we evaluate our shareholdings. Against this background we have put great energy into strengthening our focus on returns. In strictly practical terms this involves everything from sharpening our internal view of the shareholdings' value potential to developing our analysis of potential new investments. Together with my colleagues we have refined our valuation model, streamlined our work processes, increased our focus on central value drivers in the companies and put even greater emphasis on analysis of changes and trends in the world around us. For us as long-term owners it is essential to have a good understanding of the challenges and opportunities that arise out of megatrends such as automation and digitalization, focus on sustainability, energy efficiency improvement, and disruptive technologies and business models. We have also simplified Industrivärden's organization, with a clearer focus on analysis and long-term investments in our portfolio companies. These are steps toward change that will bear fruit over time.

Another important step that generated tangible results last year is that we have more clearly marked the

“DURING 2016 MOST OF OUR PORTFOLIO COMPANIES PERFORMED WELL, AND THE PACE OF CHANGE IN THE COMPANIES WAS HIGH OVERALL”

way we exercise our ownership role. This has been done mainly by the fact that Industrivärden is now represented on its portfolio companies' nominating committees by persons from Industrivärden's board or management. We also have the expressed ambition to – together with other owner representatives – actively contribute to and strengthen board nomination work over time. I feel that we significantly broadened our network of potential candidates in 2016 – a process which, naturally, is ongoing. In retrospect we can see that several new persons joined our portfolio companies' boards at the 2016 AGMs. The board nomination work is now in progress ahead of this spring's AGM season, and I feel that we have a good starting point in the continuous work of adapting company boards to the challenges facing the respective companies.

SEVERAL IMPORTANT STEPS TOWARD CHANGE IN THE PORTFOLIO COMPANIES FOR ENHANCED VALUE CREATION

As an active owner with large shareholdings we have the opportunity to influence our investments, which is the very essence of our business model. We have sharpened our focus on central issues for enhanced value creation and are working for a faster pace of change in our portfolio companies that are facing significant challenges. During 2016 most of our portfolio companies performed well, and the pace of change in the companies was high overall.

With a foundation in a successful business model, *Handelsbanken* is showing continued competitive profitability. The bank is growing organically above all in the UK and the Netherlands. In August Anders Bouvin, who previously headed *Handelsbanken*'s operations in the UK, took over as new Group Chief Executive.

For several years *SCA* has been conducting a conscious refinement of its hygiene and forest products businesses. The work now initiated by *SCA*'s board to propose a split of the company into two distinct businesses is therefore a natural step in creating greater room to maneuver and value creation. The recently announced acquisition of

BSN medical, which makes wound care products, among other things, strengthens *SCA*'s offering in the hygiene segment and creates additional growth opportunities.

Sandvik's work on increasing its strategic focus and decentralization is now generating tangible results. In 2016 the operations were consolidated to three business areas, new financial targets were set, and the company communicated its intention to divest certain non-core businesses.

Volvo is also carrying out greater decentralization, with clearer business responsibility and more efficient decision-making processes. The ambition is to focus on organic growth and to boost both productivity and efficiency through continuous improvements. *Volvo* has also announced its intention to divest certain non-core businesses.

Skanska has continued to successfully expand its project development business, but is showing unsatisfactory profitability from its construction operations. In 2016 a new business plan was set for the next five years. At the 2016 AGM Hans Biörk, who has many years of experience with the company, was elected as new Chairman of the Board.

ICA Gruppen has completed the refinement of its business and has expanded its retail business in the Baltics through the recently announced acquisition of the Lithuanian grocery retail chain *IKI*. *ICA Gruppen* is showing good stability and an improved margin in Sweden.

Ericsson is facing the challenge of increasing its profitability in a challenging market with sizable technology shifts. To achieve this, a number of thorough measures are being taken with respect to the company's organization, structure, efficiency and cost reductions. Börje Ekholm took office as *Ericsson*'s new CEO in January 2017.

Last year *SSAB* carried out conscious work on efficiency improvement and adapting the business to the challenging market situation. The rights issue of approximately SEK 5 billion combined with the internal measures that

were carried out provided needed financial stability in a challenging situation. The company's ambition is to continue growing in high strength steel and to increase the service content of its offering. Industrivärden's investment of SEK 0.6 billion in SSAB's rights issue in June 2016, has been a very good one. For the full year 2016 its Class A- and B-shares increased in value by slightly more than 100%.

STRUCTURED INVESTMENT OPERATION AND DISTINCT SUSTAINABILITY PERSPECTIVE

In parallel with the work in our existing portfolio companies, our main focus, we are continuously evaluating potential divestments and new investments. During the past year we conducted a thorough analysis of such listed Nordic companies and have identified a number of potential investments. This work has not yet resulted in any new investment, but we will act when the conditions are right. As an asset manager we always have to compare the estimated return potential for our existing investments with potential new investments.

Working with asset management is a great responsibility. By also taking on the role as active owner in the companies we invest in, then clearly we have an important societal role. We believe that corporate responsibility is imperative for long-term, competitive value creation. It is therefore important that the portfolio companies have the boards, the managements, the leadership, the organizations and the resources needed to integrate sustainable value creation into their strategies, business models, processes and product offerings. In 2016 we worked on developing a framework for our sustainability analysis in support of our active ownership. Together with our Head of Sustainability Sverker Sivall, I have personally participated in this work and feel that we have a good foundation to build further upon.

CONTINUED MAJOR UNCERTAINTY IN THE WORLD AROUND US

From a global perspective, 2016 was an eventful year with unexpected outcomes of the referendum in the UK and the U.S. presidential election. The British people voted to exit the European Union. The political and real-economy consequences of this referendum for the UK and the rest of Europe are hard to discern. After a strongly negative initial reaction the stock market recovered, which can be

interpreted to mean that a drawn-out process is expected without major near-term consequences. However, the situation may change if other important EU countries show a clear interest in leaving the union. In the U.S., Donald Trump was elected as the new President. This has led to uncertainty about the impact of future policies, such as an increase in trade barriers, changed tax policies, and geopolitical aspects. However, promised investments in infrastructure, promises for an improved jobs market, and increased stimulus measures have given a boost to the stock market. This has led to higher commodity prices, mounting inflation expectations and rising long-term interest rates. Together with a weak Swedish krona, all in all this has contributed to a favorable environment for Industrivärden's portfolio companies.

For 2017 the IMF prognosticates an increase in global growth by 0.3 percentage points to 3.4%. Even though many uncertainties remain, higher economic growth is foreseen especially in the U.S., with positive repercussions globally. Expectations are for rising interest rates, which could have major bearing on the stock market's performance. Even though companies are expected to show higher profits in the year ahead, higher interest rates will also entail a higher required rate of return on equity investments, which could put pressure on valuations. Naturally, how the overall macroeconomic development will impact each of the portfolio companies' operational performance as well as their share prices is hard to know. It is no wild guess to assume that politics, interest rates and currencies will have a significant influence on the stock market in 2017 and will thus be central topics in the macroeconomic debate going forward.

With a starting point in the current situation in the world around us, our equities portfolio, a professional organization and ongoing activities in Industrivärden, I feel we are well-equipped to generate a long-term competitive total return for our shareholders.

In conclusion, I would like to offer a big thanks to my colleagues at Industrivärden, who have made such a great contribution during an intensive business year.

Stockholm, February 2017

Helena Stjernholm
CEO