

Investment Analysis

Finnish Companies in Russia
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Author

For more information, please contact

Wilhelm Lindholm

Managing Director
+7 926 0398489
wilhelm.lindholm@capwill.com

About the report:

This report provides an overview of the recent financial performance of leading Finnish companies active in Russia. The sample consists of 15 companies which disclose quarterly financial data, representing aggregate annual sales (2013) in Russia of some EUR 5.5 billion. All companies are publicly listed with the exception of Itella. Analyzed performance metrics comprise sales and operating profit (EBIT). In the sample, 10 companies disclose both top line and profitability data (segment reporting), whereas 5 companies only disclose top line data (geographic area reporting).

Key "Finnish" sectors:

Real estate & construction is traditionally an important sector for Finnish companies in Russia. In addition to sector companies **Lemminkainen**, **YIT**, **SRV** and **Sponda**, also **Tikkurila** (paints) and **Kesko** (through DIY chain **K-Rauta**), are heavily exposed to the sector. In aggregate, the aforementioned businesses generate some EUR 1.3 billion in annual sales (2013), representing 25% of total sample sales.

Another key sector for Finnish companies is retail & wholesale trade, and logistics. Players in retail include **Stockmann** (dept stores, apparel, food) and **Kesko** (DIY, food, sports), whereas **Oriola-KD** operates both a retail and wholesale business in pharma trade. **Neste Oil** is one of the leading petroleum retailers in Northwest Russia. **Itella** specializes in logistics solutions e.g. for the fast growing eCommerce sector. In aggregate, the aforementioned businesses generate some EUR 2.3 billion in annual sales (2013), representing 43% of total sample sales. In addition to the companies covered in this report, Finnish S-Group (not listed) has an app. EUR 300 million food retail business in St. Petersburg.

Quarterly Performance Review 1Q2014: Fighting in Tough Conditions

Key take aways

1. Measured in EUR, comparable sales broadly declined, whereas half were able to improve profitability
2. The most important (negative) factor affecting performance was the weakened RUR (on avg -16% vs. 1Q2013)
3. The increased economic uncertainty and worsened macro outlook also had a harmful impact in general, but actually benefited some players in the housing sector

Company	Industry	Reporting RUS	Sales RUS	EBIT RUS	Sales (EURm) RUS 2013
Atria	Consumer staples	Segment	x	x	122
Fortum	Utilities	Segment	x	x	1,119
Lemminkainen	Real estate & construction	Segment (1.1.2014)	x	x	165
Nordea*	Banks	Segment	x	x	260
Oriola-KD	Healthcare & pharma	Segment	x	x	979
Sponda	Real estate & construction	Segment	x	x	29
SRV**	Real estate & construction	Segment	x	x	105
Stockmann	Retail trade	Segment	x	x	346
YIT	Real estate & construction	Segment	x	x	496
Itella	Transportation	Segment (1.1.2014)	x	x	239
Kesko	Retail trade	Geo area	x		359
Neste Oil	Energy	Geo area	x		361
Nokian Tyres	Consumer durables	Geo area	x		520
Sanoma	Media	Geo area	x		112
Tikkurila	Other materials	Geo area	x		204
Total					5,415

*Nordea domiciled in SWE, but largest owner is Sampo Group

**Also incl. Estonia, but impact estimated to be insignificant

Source: Company materials

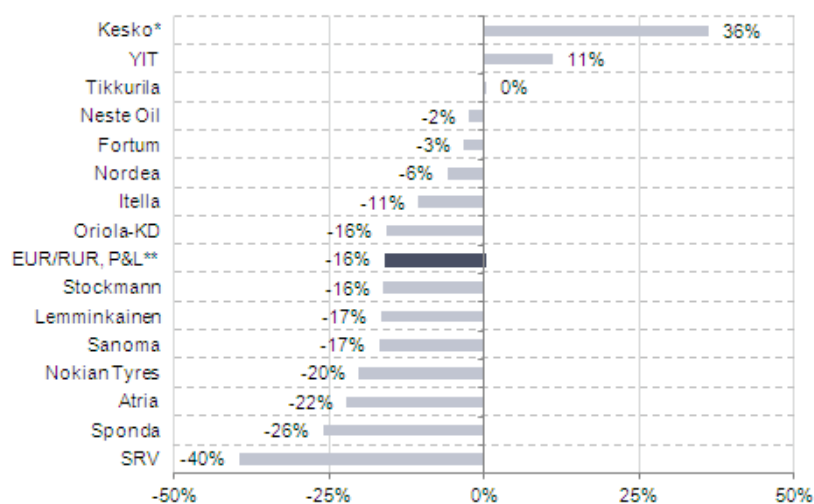
Figure 1: Analysis sample details

Weakened RUR punished top line: only 1 company was able to increase comparable sales (q-o-q, in EUR)

The companies suffered from a significantly weakened RUR during the first months of 2014. Average EUR/RUR rate (used for P&L) was 16% lower in 1Q2014 vs. the same period last year. Whereas the declining RUR affected companies differently, and sector / company specific factors undoubtedly played in, first quarter sales in aggregate were down 8%.

Kesko's impressive growth rate is explained by expansion of the company's K-Ruoka (food retail) concept to St. Petersburg in 2013. The first K-Ruoka store opened in Dec 2012, and 3 more stores were opened during 2013. Comparable sales (K-Rauta, Intersport) in the period were down q-o-q by 7%.

Aggregate sales declined 8%, or EUR 100 million in absolute terms, in 1Q2014 vs. 1Q2013



* Comparable sales excl. 4 new K-Ruoka stores -7.0%

** Avg FX rate used for P&L reporting

Source: Company materials

Figure 2: Relative EUR denominated sales development 1Q2014 vs. 1Q2013

Supportive dynamics in the housing sector

The depreciated RUR and the economic uncertainty caused by the situation in Ukraine indirectly assisted **YIT**; housing demand grew as consumers, due to FX and inflation concerns, transferred liquid assets to fixed property. Apartment sales volumes were up considerably, and prices increased slightly. Importantly, mortgage financing was largely unaffected during the period. **Tikkurila's** paint sales also benefitted from the robust demand in the housing sector, and the company was able to offset the negative FX effects by higher sales volumes and price increases (the early arrival of spring was also beneficial). Despite the favorable dynamics, it seems **Lemminkäinen** was not able to fully capitalize on the tail wind in the market place.

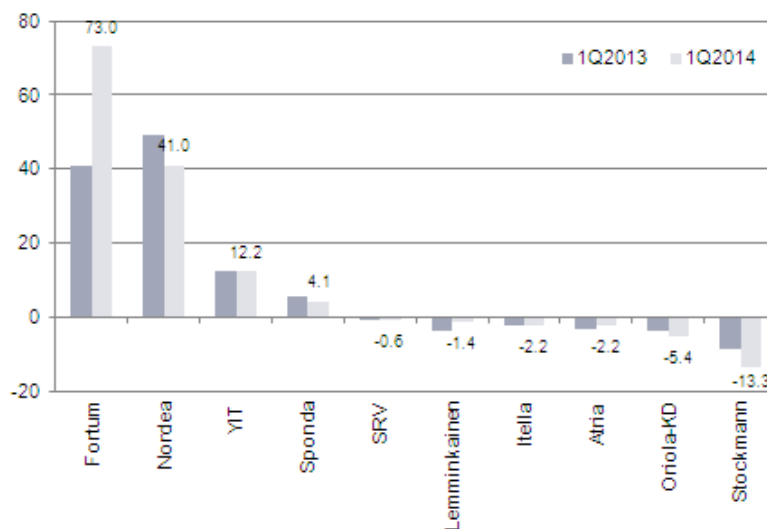
Nordea was principally unaffected by both currency rates and Ukraine events, and the small decline in sales was due to changes in fair value items. In addition to FX fluctuations, sales development of **Neste Oil** and **Fortum** is affected by changes in energy prices / benchmarks and regulated tariffs, which had a positive impact in the quarter.

A comparison of isolated periods of **SRV's** commercial real estate development business is sensitive to timing (start / finish) and related revenue recognition of individual projects. The significant drop in **Sponda's** topline was due to a decline in average occupancy rate to 88% (from 97% in 1Q2013), which was mainly attributable to an increase in vacant space in Ducat II office complex. Ducat II accounts for app. half of Sponda's property portfolio valued at EUR 240 million in 1Q2014 (CBRE).

Profit development a mixed bag: you win some, you loose some...

Regardless of the challenging market conditions, half of the (10) companies reporting profitability data were able to improve performance. It is, however, worth noting that in 4 out of the 5 cases, the improvement was a decrease of operating loss – not an increase of operating profit.

Fortum almost doubled EBIT...



Source: Company materials

Figure 3: Operating profit (EBIT), EUR million

...and a couple of minor performance improvements...

Fortum's strong performance improvement was primarily attributable to new power generation capacity receiving guaranteed payments under government capacity supply agreements, but also to higher tariffs and improved efficiency. Although insignificant in absolute numbers, and unfortunately still in negative territory, the earnings trend of **Atria**, **Itella**, **Lemminkäinen** and **SRV** developed in the right direction. In 1Q2014 the companies were able to decrease operating losses, e.g. through successful execution of operational efficiency improvement initiatives. Excluding a large (positive) loan loss contribution in 1Q2013, **Nordea's** comparable operating profit was slightly up.

YIT was unable to convert the positive sales development to a corresponding profit increase, e.g. due to sold apartments on average having a lower completion rate. In addition to the mentioned drop in occupancy, **Sponda's** result was also negatively affected by a property tax increase in Moscow.

...but also some casualties

The result of the companies with costs mostly in EUR/USD and sales in RUR were hit hardest. **Stockmann** and **Oriola-KD** fall into this category. Oriola-KD also cited the intense competitive environment as a contributing factor to the weakening profitability. Following the disappointing first quarter, Stockmann in the end of May announced initiation of a "strategy review" on group level, which may also result in changes to operations in Russia.

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Contact us

Capwill LLC
Advisory | Investments
www.capwill.com

Wilhelm Lindholm
+7 926 0398489
wilhelm.lindholm@capwill.com