

Questions and President and CEO Matti Halmesmäki's answers at Kesko's Q3/2014 media and analyst briefing on 22 October 2014

Minna Nalbantoglu, Helsingin Sanomat:

Your have been losing market share in the food trade this year. Can you say how much and why?

Matti Halmesmäki: Nielsen will publish the official market shares in March. Based on the Finnish Grocery Trade Association's monitoring data, we have estimated that our market share has slightly declined, but less than one per cent in any case. The reason must be that not all of our stores have been able to offer customers what they appreciate these days. All the more so, because customer behaviour has changed. Generally speaking, we have the best stores and the most satisfied customers in this country. But obviously, there is too much variation among the K-food stores. What is more, price has become increasingly important, but our message will be that quality is not unimportant either and all stores are not alike in terms of quality. Quality is about Finnish products, extensive selections, service, fruit&veg, bread, service counters etc. But we neither criticize nor praise our competitors in public.

Jouko Kyytsönen, Maaseudun tulevaisuus:

You said that cheese slicing is now over and structural reforms are needed to achieve higher operational efficiency. What will they be?

MH: Well, they will be planned further under Mikko's leadership. But a stronger non-food operator is needed to generate efficiencies and develop the operations. Transferring K-citymarket to Kesko Food is a typical step toward improved operational efficiency. A shared customer promise will enable more flexible processes in marketing, selection management, logistics etc. However, responsibility areas and profit centres must be clearly specified for the different product lines. Principals also play a significant part in the implementation at store level and customer interface, especially in the car trade. In other words, a number of elements have to be combined successfully for efficient operations. We have already achieved lots of savings in IT and efficiencies from sharing platforms among different business areas. In today's web world, we need to build comprehensive, real-time product data registers in cooperation with suppliers and retailers, and we must also have information about our customers for use in customer encounters and customer service. Digitalisation is not a threat for us; who could be a better content producer than any of our 1,100 K-retailers equipped with top quality tools! I see much strength in our present structure; with the variety of our product lines, for example, we can serve customers in all situations of their lives. But the requirements of this period of transition are undeniably heavy.

Pirkko Tammilehto, Kauppalehti:

Where do you think a buyer for Anttila can be found?

MH: There is always a buyer but the price must be right too. Our CFO Jukka Erlund is canvassing potential buyers with advisors. If a buyer is found, the news will be released. According to our policy to provide all investors with equal information, we have openly expressed our intention to sell Anttila. We are not simply waiting for a buyer and have launched major improvements which will generate a major profit improvement next year. Our warehouse in Kerava is one of the most modern warehouses in Europe where orders from individual customers and department stores are filled by robot pickers. I'm not sure if the new management will actually want to sell the warehouse, because it provides major development potential for the product lines of the building and home improvement trade and the non-food trade as a whole.

PT:

Is it possible that if a suitable buyer and a suitable price are not found, Anttila becomes an online operation with no physical stores at some stage?

MH: There is no such plan, at least not at present. The department store volume is so big and the multi-channel aspect so important that such a change would perhaps not be wise in this situation.

Riikka Kalmi, Taloussanomat:

How much was Anttila's loss for January-September and what was the change from last year?

MH: I'm not sure about publishing such company-specific figures, but the loss had grown somewhat. This is partly because of the ongoing changes and because the process of closing so many department stores is not very simple. And the development of the information system, involving 80 people working in the SAP project, has demanded a lot of resources.

Arto Jaakkola, Kehittyvä kauppa:

What is the situation in Kesko's participation in the Fennovoima project? It has been announced that Kestra Kiinteistöpalvelut Oy will not participate in future financing of the project. But nevertheless, there has been some speculation about Kesko's participation.

MH: We have published a stock exchange release saying that we will not participate in its future financing because of uncertainties in the financial, contractual and schedule prerequisites and increased risks.

AJ:

When will more detailed information about Kesko's main office building be available? In other words, will Kesko's main office building remain at Satamakatu 3?

MH: Plans are being prepared. The present city plan is very old and interpretative but it also allows apartments. In preliminary discussions, the City of Helsinki has been very positive. On the other hand, there is a willingness to develop retail operations and other services on the site. These alternatives are now being examined. Since Kesko Food moved to Ruskeasuo, there is no immediate need to make decisions. But in my opinion, it is possible that the building will not be in office use in the future.

Mika Karppinen, Evli:

You just said that Anttila's profit is expected to improve significantly next year, but the guidance promises steady profit performance. What are the major risk areas where Anttila's profit improvement can disappear?

MH: The overall guidance is an aggregate of all divisions. But when 12 department stores are closed, the loss will decrease significantly, coupled with the other enhancement measures already taken. Other contributing elements include the revision of selections, changes in management, a new president etc. Kesko's guidance is not dependent on Anttila, which only accounts for 4% of Kesko's net sales.

MK:

I've understood that Anttila's losses amount to tens of millions euros. So, a significant improvement in them would be reflected in the Group level figures too.

MH: Yes, you're quite right there.

Minna Nalbantoglu, Helsingin Sanomat:

Has the deterioration of the economic and political situation affected your expansion plans in Russia? And how have import bans on Western foodstuffs impacted your food trade in Russia?

MH: In May, we discussed a whole day with Kesko's Board of Directors about our strategy for Russia. We decided not to make any panic decisions. Instead, we will complete the projects underway including new construction. Naturally, we realise that although the current situation also provides opportunities to acquire good business sites at low prices, we may be facing an extended economic recession with a weak rouble and political sanctions with no knowledge of their duration. But as a whole, we will continue our operations in Russia relatively normally; the fact is that profitability requires a certain volume in the St. Petersburg cluster. Project launches are monitored more closely these days; before a planned project is launched, the local management verifies the go-ahead from us. Our Russian food stores are full of products and only minor changes have taken place in the selection: banned products have been replaced by lots of local products which

are often cheaper, whereas the quality of, for example, salmon from Murmansk is different and the price is clearly higher. There are no significant shortages of products. When I was opening our first food store in Russia and told the city management representative that local suppliers could now have their products included in good selections and increase their sales, at least that person was of the opinion that it was important that the store is selling Finnish products. And Pirkka products, for example, have had a very good reception, but some of them are now under export ban and have been replaced by local or imported products.

Jouko Kyytsönen, Maaseudun tulevaisuus:

Your capital expenditure has clearly increased from last year. Where has it been made? And your agricultural trade in the Baltic countries had declined. Are you going to do something about it?

MH: The profit performance of our agricultural trade is still strong, but sales have declined and consequently also profit somewhat. But the Baltic agricultural and machinery trade is very profitable. Lithuania has suffered most because of the sanctions coupled with EU subsidies, but Estonia exports milk to Lithuania for processing and export, which has had a negative impact. But never before has Kesko's agricultural trade been more profitable than today and it has also increased its market share.

As for our capital expenditure, in my opinion, it is relatively low compared to our cash inflows and depreciations as well as our capacity for capital expenditure. If we say that it was very low last year, it has been reasonably low this year. Large units in Russia are roughly as expensive as in Finland; the total capital expenditure in Kamenka, for example, was around €60 million.

Pekka Pansu, YLE:

Since online sales are growing, what is their share now and what do you expect it to be in, let's say, two or three years?

MH: Online sales are growing by two-digit figures. Online food sales will also increase, although regional differences will remain. Our multi-channel approach enabling customers to order goods for collection from stores, the click&collect system offered by the building and home improvement stores, our online services available to customers, etc. have great potential. Whether the ordered goods are delivered to home, physical store, post office or some other place makes a difference in terms of logistics solutions. Competitive online services are a matter of life and death in the trading sector. Of course, there are product lines with high average prices and well-known brands, like in electronics, where the price level will become harmonised as customers compare prices. I expect that in response, retailers will develop own brands which makes price comparisons more difficult. Naturally, food transport chains and product identification is not as easy, which keeps the share of foodstuffs smaller.

PP:

What is the outlook for Russia?

MH: It is impossible for anyone to forecast. I'm sure many operators have gone there expecting that Russia will develop as a vast market economy and become wealthier. A population of 145 million with a good level of education provides strong potential for development. But no one can tell what kind of stages will be involved and how democratisation will be integrated into them. Anyway, I don't believe that the old system will be restored despite occasional concerns and phenomena.

In case there are no more questions, I wish you all a nice autumn and hope you shop at K-stores. Thank you!