

Conference Title: YIT CMD 2017, Esa Neuvonen, CFO

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Esa Neuvonen: Good morning. It was just about one year ago when I first time took part in the YIT's public event. That was a CMD in Bratislava. And, of course, I was about to start later on on that year. So, I think that one could start, that when joining a 100 years old company in established industry that you could have let's say a nice time, introduction period, getting to know the company, visiting different businesses and so forth. That didn't happen. I must say that it's been really a busy, busy period, but very nice one.

I have today two topics. I'll give an update on the finance health and then I'll discuss a bit about Partnership Properties, the new segment to be established in the beginning of next year. But first I'll start with a little bit of reflections, how the first year has been, how the company has looked like. Of course, when you join the company, I knew that the strategy was revised and we went through the different viewpoints with Kari before starting, but it's always kind of something that you aim to go deeper in that how the company really is. And I must say that it's been very impressive that how good a foundation people had made different units had made, how seriously they had taken in the task to release capital. So, it wasn't just a kind of a onetime rehearsal kind of a releasing money, but they were kind of long lasting solutions. And these reasons which we made. So, very good foundation for that.

The other angle what really impressed me was the, let's say, how much energy the new strategy brought to company. And, of course, started during the strategy process. Very concrete, I would say, very unique innovations made within the company. By saying that I mean Smartti concept of which we have now already a second phase is coming through the housing design. And as Kari mentioned the Smartti prefabricated modules can be seen outside. But also I think that actually, the Tripla project we very often mention that that is a source of innovations in many angles. It's, of course, a technical challenge, but that is also a commercial innovation connecting the different

traffic junctions and so forth, creating a truly unique area for the city. And that is one of the topics that Juha Kostianen will be discussing later on. So, kind of a – in that sense, I think that a very good basis for growth. But I must say that for me personally, an eye-opener was the fact when I realised that what a unique position YIT has coming from the investor perspective that suddenly you have extremely good visibility on the projects that are in the market and how you could take advantage of those going forward. And I think that was a motivation personally for me, of course, kind of supported the ideas from the Tripla and so forth, to really try for something like Partnership Properties. That wasn't the name at that time, but the discussion then continued from there on. But – so I will say that positive surprises, very, very impressed by the way that the organisation actually was energised from the new strategy.

Then I'll start going through the financial position of our different businesses, our backbone, Housing Finland and CEE. Actually the market started improving already last year. So, supporting the profitability has been improving for some time, supported by the improvements made in the sales mix, giving less discounts to the investor customers and very good development in the CEE countries.

So, one of why these backbones representing last year 41% of the revenues is in good shape, the market, as Kari discussed, in a good condition. Of course, there are ambitions going forward; we still need to improve the capital efficiency on the area, improve, for example, the plot turnaround in the area to further improve the return on capital, capital employed.

As Kari mentioned, some new data as well, regarding housing CEE, very often asked area that how we are actually doing as this is a combined report within the unit. But as you can see, the profitability has really developed nicely. Or I think that has been an impressive development that fairly fast we have been able to kind of really establish the operations and actually create better margins than what we have in the Finnish operations. So, since 2015 already, the average operating profit on CEE countries has been above the average. And I think that is a very fast

jump up for new geography. Of course, when we are in the growth phase, that ties a lot of capital; so, the return on capital employed that is on another level. Very good growth in average if you look at start-ups, the growth has been 27%. So, good development in this area and has been supporting the development.

Housing Russia, as Kari went through, weak sales this year after ending of the government subsidy programme and also the speculation around currency development. And in Q1 and Q2 the sales were over 30% lower level than in 2016. Return on capital employed clearly negative, but gradually the project margins they are improving also here. I think it's good to look that it has been a good achievement from the organisation when we look at the green part of the chart, that how the sales compared to previous quarters how that has developed. In the beginning of last year, the sales came up 24% and continued on that level throughout the year. And as you can see that since third quarter already, the profitability was back on the profitable side. And then, as Kari mentioned, in the beginning of this year, the sales truly dropped, putting us back on the negative. But again, the organisation adjusted and we are currently capable of creating positive margins even with these conditions. But the sales, they have improved in the third quarter compared to the beginning of the year, but still clearly below last year's level. So, a challenging market but I think that good achievement from the organisation to adjust on the conditions.

Business Premises and Infrastructure, profitability came back on a satisfactory level on the second quarter. There have been tenderings on the market, we haven't succeeded on those. The margins they have been truly tight on those and not meeting our target levels. But I think that when you analyse this segment, it's good to notice that we have actually two different business models mixed here. We have investment type of a role in Tripla and we have the underlying project business. And now when you look, the return on capital employed, that is a combination of both. And I think that is one reason why we are also establishing this Partnership Properties to give clarity on the different earnings models and really show that how the project part is doing.

Return on capital employed has been developing nicely in Finland, gradually going upwards in Business Premises and Infra, kind of a steady development, but, as mentioned, we have included the investment portion of the Tripla joint venture. The main challenges rely or remain on the Russian operations. Clearly on a negative, but, of course, this is burdened by the write down which we made last year. If we take that into account, we are slightly on the positive side but clearly not meeting the group level targets. So, there is work to be done, as in Kari's slides, to reduce capital and improve the profitability going forward. But, of course, that is limited under the current market conditions.

Cash flow, we are more or less on the targeted level. We are aiming to keep the cash flows on a positive after dividend payout, but this is kind of optimising task as we are growing, we continuously need to optimise that; what is the mix, how much do we sell to the investors to balance the cash flow, and how many projects do we start. So, that is a constant work for us. Order backlog still on a good level, the latest increases on that were during the third quarter. We got contracts on water towers in both Vantaa and Raahe. And then we made a maintenance contract[s] worth €100 million. So, fairly stable position on those.

The status regarding financial targets, we have let's say semi-good position there on growth. We have been meeting the targets 13% growth in the beginning of the year, supported by growth in especially Housing Finland and CEE. Return on investment on red, excluding the write down, we are a bit above halfway. But, as discussed, two of the three segments, they are in a fairly good level. Russian operations burdening this one. Operating cash flow okay, equity ratio below our target level, but has improved from last year. The dividend payout has been on a higher levels. So, kind of in a semi-good status regarding the financial targets.

Then about guidance, remains unchanged. And I would like to repeat, the messages which we gave on the second quarter reporting, the message was that the third quarter will be only slightly better than 2016, meaning that the last quarter will be strong supported by two elements: the

targeted closing of Kasarmitori project and also the good sales from Housing Finland and CEE, as the projects as they are getting closer to completion and as the sales rates are coming on higher levels, then the combined profit is then supporting the end of the year. So, the guidance for whole group at revenue is estimated to grow between 5-12% and adjusted operating profit between €105 million to €115 million. And I would also like to remind, as we have communicated earlier, that the financial expenses for this year, they will be on a clearly lower level than a year ago supporting the earnings for the full year.

Then the new Partnership Properties segment to be established on the beginning of next year, I'll start with the background, what has been the motivation for this. Of course, driven from our strategy, we are aiming to grow especially urban development is the trend what we are aiming to look for. And as we have communicated, the urban growth will be the growth engine for the company. To get the engine going, of course, we need to take certain steps which partially we have already taken. We established on a group level urban development unit as mentioned already earlier. New function to be or thing to do is to establish a plot factory, so kind of now we are creating and increasing the capability to create good ideas. But then, of course, through Partnership Properties we are aiming to increase our capability to really take the projects forward, not alone, but together with investors and us, then supporting our growth. So, it's the kind of you need to take steps to get the growth engine going forward.

What are then the targets of the new segment? Of course, improve our growth capability as mentioned, being able to take part on the larger projects, being able to manage our balance sheet, but also to improve the visibility on the assets, what we already today have on our balance sheet. I think that there is not sufficient information given for you to really value that what we already have today. And on the longer run, create a portfolio of a stable cash yielding assets. So, those are the targets. And from the lets say concrete perspective, we are aiming to increase our investment capability today, the combined capabilities; €1 billion, we are aiming to double that, to €2 billion. And I think it's good to open up and define what do we mean by investment

capability. That means that is the combined sum of equity investments made by us and our partners, together with the debt that is directly coming on a project level. And to give an example, that of the current €1 billion, Tripla mall is representing €600 million. In the project we have – together with our partners, we have committed to put €300 million worth of equity and then we have a loan package worth of €300 million. So, that's what we mean, to double that type of an investment capacity by the end of 2020.

Roles of the new segment, we are not aiming to build a massive organisation, rather creating an efficient team of expert and relying on the capabilities, what we already by now have in group, and also then creating partnerships. But if you kind of start from the investor point of view, what we are aiming at is to create readymade solution for investors, that all of the pieces would be in place. A great idea, rent it out, lending in place, legal structure, maintenance of the projects. So, kind of as easy as possible for investors to come in, but with very higher level of transparency, very kind of solid reporting and valuation for the assets. And I think it's kind of very rare that when establishing something new that you can have such a fine start for the creation of the new function. We have extremely good starting base, great projects created by the business units and also kind of a nicely coming from the, let's say, different risk profiles. Mall of Tripla has been mentioned kind of unique commercial asset, but on the other hand also, as an example, E18 Hamina-Vaalimaa highway kind of very low-risk investment, long-term contract, state risk more or less as a counterparty. And then under development, Tietotie office, the school renovation project which is still under discussion and negotiation, but let's see can we succeed on getting this also to the asset base. But very good projects, very good successes, and I think that you couldn't wish for a better start for creation of a new function that you would have such a good and concrete examples to investors, that this is what we can create, this is the value that we can establish.

As mentioned the personal motivation for me more or less was this unique position in YIT. When I look from the investor angle, the situation, it's very often that you have a very limited visibility on

the projects what are on the market, and they come occasionally and you cannot kind of foresee that what would be then coming at the end of the year or next year. You have to kind of select on the individual case that do you come in or not. In YIT, we have a good visibility on different asset classes, on different geographies, on different types of risk profiles, and that actually can create the capability to really plan forward of the building up the asset base. And then kind of very nicely fit into our strategy, from the traditional construction company's point of view. You're fairly distant from the customers. Now, as we kind of step in the owner role, we can kind of truly learn that how we could improve still the product and what services could we built on for our end users. So, kind of this is the uniqueness that we are able to establish Partnership Properties next to, I would say, outperforming project development capability. This combination kind of really kind of struck me when we started discussing on this topic.

To give you some flavour how we see the different portfolios, we are aiming to create different asset classes, different risk profiles so that we could lure in different types of investor partners that they could themselves select that what type of a project do they want to take part in, what type of risk profile they want to then participate in. Development assets, meaning more or less commercial assets in different phases. It could be something like Tripla, still on the development phase, not yet producing rental income, or it could be something further on the development path. Residential assets could be also different geographies, but extremely good capability of really designing the residential product made for rental use when it comes to layouts, when it comes to material selections. Yielding assets kind of on this category we have for example the infra type of assets, very low-risk yielding assets with a longer horizon, but I think that they are not also this type of available in the market. So, kind of a, we are aiming to really have a good diversity on the offering what we are aiming to discuss with investors.

Then a little bit about, let's say, the value creation, how we see this role creating value. If you looked at how we are operating today, very often we are holding the asset in the beginning, during the development period, then aiming to make a contract with the eventual investor. And

then our role in the earning is the project margin in what we are then receiving. We are aiming to create flexibility, how long do we hold on the asset. If you look from the asset value point of view, it usually takes something between 5 to 7 years really to kind of have the peak value of the asset. Then you have kind of a gone past, the phase that you would have the technical risks there, or the commercial uncertainties like in the Mall of Tripla. Of course, before we would have any of the part of the premises rented out, the value is not the same when we have it very far away on the renting path. So, that's how the case would go on the positive project, that it will take some time when the fair value goes above the project cost and the land acquisition cost. And this is the flexibility what we are aiming to create together with our partners, that we can actually choose when what is the optimal timing for the divestment and then through that create value.

The other angle is that when discussing this type of role, if you would alone start investing on the projects, for example, Tripla mall, €600 [million] project, if you would alone invest in that one, that would be it for the project development, for some year, that would be – that's a kind of a large scale development. So, we do not have the resources to kind of take all of the opportunities, what we have on the market. But when working together with partners, having maybe 30-40% ownerships on the project level, then actually what we consume is only 15% to 20% of our balance sheet, compared that we will take a whole role on our own. So, this is kind of a very simple math there but very nice fitting to our thinking. And I think that kind of not this type of operations existing on the market.

A few words about reporting of the new segment. Starting from first quarter 2018, as mentioned, one of the ambitions is to give more information about the assets. So, of course, kind of give information what type of projects do we have, but also give additional details on the project so that it is possible from outside to really kind of make a justification that how the asset is. It could mean that we would give then additional information about occupancy rates and the development of renting or rent levels and such. But also we are aiming to give some information on the project pipeline so that there could be also visibility that's how we are taking this forward. From the

valuation perspective, when the asset is completed, when that is creating rental income, then we are aiming to start fair valuation of the asset. We are aiming to have very good transparency, very good visibility on that one, and that's why we are aiming to do that together with external appraisers so that we could have common practices, good credibility on the value, on the fair values.

From the income statement point of view, when the asset is fair-valued, when we are consolidating the joint ventures and the underlying assets, then actually the fair-valued changes, they will come through our profit and loss. And also, currently, for example, in the Tripla case, we have to eliminate our ownership share of the project margin. When the asset is ready, when it's yielding rental values and we start the fair valuation, when we are consolidating the joint venture assets, actually indirectly then the project margin comes through to our profit and loss. So, this is kind of very important, that without actually selling the asset we can have the visibility on what was the value created through project development but also through normal project phase.

On Tripla, I think that I went through actually these topics, but the aim is that when the asset will be ready, regarding Mall of Tripla, by the end of 2019 or beginning of 2020, then we will start the fair valuation. And that would have an impact on the income statement. Also as mentioned through this consolidation of joint venture assets, also the eliminated project margin would be coming through. As mentioned, the target is to create flexibility for us to really decide what is the optimal timing of divesting the asset. Most probably the true value of Mall of Tripla is not coming on a first day when the project is completed. It will take some time to really kind of show that that is unique location and people get familiar with the projects. So, therefore, we are giving ourselves the flexibility really to kind of think what is the optimal timing for divestment.

But to summarise, what are the benefits, what is the idea of the new segment? Improved growth capability, improved capital efficiency. But also we have an opportunity to really create new earnings models through ownership and based on the services as we take role in a new position

as an owner. And also that we do not – I think that this is creating an efficiency, that we are not creating the same structures, same things again and again for each project that we can repeat the legal structures, the funding ideas when we build partnerships with the investors.

In reporting, very important that without really divesting the asset we can have visibility on the fair value of the asset, and also in the long term we are looking to create balancing stable cash flow yielding operations. Thank you. That was my presentation. And now I think that there is some time for questions.

Ari Järvinen: Yes. Ari from Danske. So, a couple of questions on this partnerships initiative, like if you say that you would have capacity to increase the investment capacity from €1 billion to €2 billion in the next three years or something, does it mean that you have to hire new people, get new costs like to create this kind of potential for your company?

Esa Neuvonen: I think that is the beauty of the whole thing, that actually what we are creating is, let's say, efficient team of experts. We are focusing mainly on the capabilities to preparing investment cases, capabilities of preparing the funding and legal structures and also capabilities to revalue the assets. And then on the other areas, when it come to, let's say, investor sales, renting out the apartments or creating renovations or preparing those, then we are aiming to rely on partnerships. Internal partners, but in some cases, I guess, creating also external partnerships; but no kind of massive need to create organisation. We are more kind of talking about efficient team of experts, being able to create partnerships and take advantage of all the skills what we have in house.

Ari Järvinen: Okay. And then I'm really pleased that you are giving us more visibility into the commercial development projects and giving numbers also for it. So, that's a good thing. But then I have to ask that, should you have a stronger balance sheet and good projects in the larger scale where the competition is much lower, would you really need those joint ventures if you had

a stronger balance sheet?

Esa Neuvonen: Well, I think that is the whole idea of partnerships. I think that as we are, anyway, into roles that we are creating projects and then also in investor role, that if you then kind of select, let's say, of course you would think that these are the most interesting projects, how do you then kind of sell the other projects to the investors? That would be a kind of a pretty heavy task to convince that these are equally good. But I think that when we are in the, let's say, minority owners' role, then that is very strong message that we believe on those projects. Everybody understands that our balance sheet doesn't kind of allow us to take part in all of the projects. So, I think that our – in the core of our strategies, working together with partners, that means sharing risks, but it means also sharing profits. So, kind of this very nicely fits to our thinking.

Ari Järvinen: And I suppose this Kasarmikatu too has been a really successful like project because the location is top notch and it's fully rented now. But have you – can you envisage that there could be some like problems or kind of like differences of opinion maybe if you have several parties that went to exit a project? When would you be selling your part or are you kind of like confident that you're happy to manoeuvre in a flexible way that if you feel that you need the cash flow, you want the exit, you can do it and you're not restricted by the other parties.

Esa Neuvonen: Very good point. We have kind of also come to the same conclusion that you can never find, let's say, a group of investors that would have exactly the same needs and same ideas. So, kind of we need to create a structure that – where you can flexibly exit and also taking the others into account. So, that's what we are planning to have.

Ari Järvinen: Okay. Thanks.

Esa Neuvonen: And then.

Hanna Jaakkola: No more questions from the audience? No? No questions from online either.
So, let's have a break now.