

President and CEO Matti Halmesmäki's answers to questions at Kesko's Q1/2014 media and analyst briefing 24 April 2014

Susanna Jääskeläinen from STT news agency: It seems that the great transition underway in the home and speciality goods trade is gaining speed and you have already made some major arrangements. What is the future outlook: will you have more of such arrangements, loss of jobs and store closures, or is the worst over now?

Matti Halmesmäki: This digital transition will certainly accelerate and we are doing very hard work in this sector. We have the best situation in the world in the sense that we have information about 3.7 million customers in our registers. And naturally we also want to act responsibly. Privacy is very important for us. Electronic marketing cannot be done without permission from the customer. We have seen that customers are willing to give such permission, if they feel that the marketing content is meaningful. And the other question is what kind of electronic communications to use with customers. E-commerce, including food retailing, is on a strong growth. The home and speciality goods trade is naturally in the front line here.

But there are certainly also many other factors to this. The current economic situation in Finland has its impact, but we also have to consider how to improve our own operations. NetAnttila continues to be one of the leading online stores. I believe that Finnish online stores will become more popular, because quite a number of customers have had disappointments with foreign online stores – with their payment systems, product quality and returns. But I believe that one major issue will be the fact that only few customers are aware that their online purchases are also subject to VAT and customs duties. And I have understood that customs authorities are going to have more say on these direct purchases from abroad.

This kind of a reliable operator like us and our comprehensive network, either as a delivery network or having goods on display, when shop assistants can use various electronic tools to increase the selection with colours, sizes, qualities and brands. This requires extremely good systems; the customer information system alone is not sufficient. We need to have shared product information registers, expertise and systems with our suppliers to make everything work; so that manual work, such as e-mails to customers, is no longer needed.

But we have gained excellent experience about service booking systems in the car trade, for example. This electronic world is everywhere; for example, you can book test drives online and so on.

K-citymarket is by far the biggest channel for selling both groceries and home and speciality goods. If our selections are in order, I believe that customers buying for groceries are also willing to shop for high-quality home and speciality goods for themselves and their families.

The food trade will not go online as fast and widely as has been the case with home electronics and other home and speciality goods. But we also see it as an important target for development. And the business operations of K-citymarket also need enhancement and changes, when it comes to service promises and selections.

In the sports trade, discount stores often try to sell the same brands of running shoes as speciality stores, but when you are running a marathon and approaching the finishing line and your shoes no longer feel good, that is when you need the confidence. Only a top salesperson and a top store chain can really provide the support and confidence the customer needs and is ready to pay for. But, of course, there are many brands and customers are comparing prices. We have new competition which needs to be taken seriously.

We have transferred most of Musta Pörssi home electronics business online and have had high growth figures. Analytics on customer behaviour online need to be developed, and the situation is not gloomy in this respect. People often want to have simple truths when things are much more complicated. For customers, the situation is just splendid: worldwide selections at competitive prices across Finland. It cannot be denied that this is a transition for the trading sector; I'm the last to underrate this. But we have to proceed from the current situation. This transition has been really harsh and will no doubt continue to accelerate. We have to look at our business by concept.

Even shoes are sold widely online, but I believe that traditional stores also make it – footwear is not easy to sell online. And it seems that in clothing, in some of the most difficult goods, the return percentage may be 30 or even 50, which makes the equation extremely difficult for profit generation. They represent a pioneer approach, customer service, a learning process. There are not many operators in the world with profits from e-commerce. It seems that there is some tendency to overestimate online stores' profit-making capacity. If a store collects goods using normal routes, that is, paying the store expenses, collecting, packing and delivering goods for customers and then a third of them come back – margins need to be very high to make business profitable. It might pay off to provide this service for the best customers, but our online food store, ruoka.citymarket.fi is based on deliveries made from our central warehouse and combines deliveries to senior citizens in home care in the cities of Helsinki and Vantaa. I believe that in terms of volumes we are today the largest home delivery operator, which means that we can increase logistical efficiency by combining online sales to households with home deliveries to senior citizens. I trust that home deliveries to senior consumers will increase because old people want to live at home as long as possible and have food service paid either by them or by the municipality. And this is a factor that will increase volumes. We also won the competitive bidding in Turku, but a complaint made there has postponed the start.

And K-stores have also started by serving their own customers. In the Helsinki region, we already have some and will have more retailers who collect goods to wait for their customers to pick them up. We have systems for this across the country, so that customers

won't have to wait at home at certain hours and they can also save the transportation charge.

This was a short review to the world, which is undeniably also reflected in Kesko's figures. It is also part of our responsibility that we take e-commerce seriously and act accordingly, as it is no cyclical development.

Anneli Hertsi from Kauppalehti: What kind of options are you considering in Russia, is it possible that – when you do have money – that you would proceed faster in this situation? There seems to be one problematic business site in St Petersburg, but is it of importance?

Matti Halmesmäki: There is certainly a fair amount of problems in every firm and in various units. There has been much public discussion about this Pushkin site; the town plan is in order but there has been talk about whether it is a suitable site for a food store. There has been talk about a food store and a building and home improvement store. It is not even visible from the culture area, so I don't know the interests of the party who has made a complaint in this individual case. One has to be pragmatic in this business; risk management is an essential part of business and we cannot say that we are hitting the gas pedal. There may be some overreaction by some operators. I said at the Annual General Meeting that we have a capital of €340 million in Russia. Our intention was to include Russian properties in our real estate fund, but we are now backing down, because many investors do not want to have Russia position in real estate investment now. Or if so, their leaseback requirements are unreasonably high compared to how we see the risk.

Kesko's Board of Directors has made decisions on several targets. When it is time to sign the agreements, we will see what the situation is. So far, we have proceeded as usual and today I will have a meeting with the President of Kesko Food on whether to sign the next agreement. The seller of the property reduced the sales price markedly and I will probably give permission to sign. We have to have a long-term approach but, on the other hand, take the market development into account. The supply of good store sites will probably increase there, because of related speculative demand. And the risk-taking capacity is now weakening there. But nobody can have exact knowledge of what is the right action just now.

As for Intersport, we are looking for a retailer model there and, for that part, distributing the risk and expanding the business.

Thank you, have a nice spring and the first of May. And remember to visit K-stores!