Sanoma Oyj Full-year result 2010
Wednesday, 9th February 2011
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Chaired by: Harri-Pekka Kaukonen

Harri-Pekka Kaukonen

Ladies and gentlemen welcome to the Sanoma House Auditorium where we will be presenting the Sanoma full year result. But before that I would like to introduce our Chairman, Jaakko Rauramo.

Jaakko Rauramo

Morning.

Our Head of the Media Division, Eija Ailasmaa

Eija Ailasmaa

Good morning.

Our CFO, Kim Ignatius, who will present also today.

Kim Ignatius

Morning.

And then the Head of our Entertainment and TV operations, Anu Nissinen.

Anu Nissinen

Good morning.

Anna Tuominen

Warmly welcome on my behalf as well. Just a few practicalities before we begin. This will be a live webcast on sanoma.com and on demand there as well later on. We will first hear presentations from Harri-Pekka Kaukonen and CFO, Kim Ignatius. And after that we'll have a Q&A session. We'll first take questions here in the room and after that over the phone lines. The presentation material is also available on sanoma.com for those of you live there. And while we start the Q&A session please wait for the microphone before asking your questions. Harri-Pekka.

Harri-Pekka Kaukonen

Thank you Anna. Ladies and gentlemen it's a pleasure for me to be here for the first time and presenting Sanoma's full year result. I will go through the Q4 and then the full year result and then share some comments regarding the future outlook. If I go to Q4 first. If you look at the absolute revenue numbers there was a decline from the previous year, but when you adjust for the changes, the structural changes, mainly the divestment in Humo, the growth was about 1% point. The operating profit in absolute terms decreased from the previous year, but there I would also like to point out the impact of the structural changes. On an operational point of view all other divisions reached our internal target, but the trade was hit by the changes and the opening hours and the performance in trade did not fully reach our expectations. In addition, since the markets were rebounding we also wanted to maintain also the future profitability and stepped up marketing activities to support our main titles and operations. In addition, Kim will explain in more detail, but there are some items regarding ICT depreciations and that had some impact on the non-recurring EBIT.

The last quarter continued the development in the advertising market. We had substantial growth in most of our markets, especially in Finland, the numbers of both TV and online markets grew in double digits, and also the job advertising which is the key revenue generator for Helsingin Sanomat, that was growing at a rapid pace. During the crisis in 2009 Sanoma undertook a number of cost efficiency improvements measures, and you could see the impact also in Q4. We had focus on expenses and kept those under control. You can also see in the comparable numbers how the impact of investment in advertising and marketing spending that I mentioned was substantial during the fourth quarter. We also enjoyed lower paper cost than the year before which has to be taken into account when analysing the Q4 results.

If we look at the full year performance, we would characterise it as a good achievement and that we’re happy with the performance improvement. The net sales on a comparable basis grew somewhat, but especially the EBIT performance was a substantial development. This result improvement, I’d like to point out a few factors that contributed to it. The market rebounded; the advertising market grew in all of our operating markets. I already mentioned the impact of lower paper costs and printing costs, but we also did and benefitted from a lot of the development effort that has been done in all our units. And that has led to the fact that despite the lowering circulation volumes, we have been able to compensate to a large degree the decrease of circulation. That has been something that we’re very proud of. Last year was also characterised by a strong development in online products and applications and services. A number of new iPad applications were launched with interesting prospects. We are at the very early stage, so the revenue impact and the financial impact is small to date. But I think, for example, in the area of Helsingin Sanomat, I think this iPad application is a very interesting additional benefit to our multiplatform subscription offering.

Another point that I’m really glad about is how our online reach continued to grow. We have about 80% reach of the online population in Finland, Hungary and the Netherlands and also in Bulgaria. And I think that’s important for our future development. As a curiosity too of our iPad application, as you see in this chart the Viva and the Story, were voted number two and three in an independent poll of iPad applications in December. The performance improvement led also to healthy cash flows. Cash flows have been one of our group targets since last year and we’re glad to see a step improvement on that front as well. Earnings, where both did compare to the previous year and a big contributor here was of course the impact of the Welho deal. And the dividend proposal is €1.1 and I will get back to that point a bit later in my presentation.

A few words about the outlook, generally not so much about the macroeconomic environment, I think we also watch that very carefully, especially the consumer confidence is important. And obviously since we have a big share of advertising revenues, the economic development place a big impact as was already seen last year in many of our markets. But we are cautiously positive regarding the macroeconomic in most of our markets. More specifically about some of our key markets, last year was, I'm very happy to say, that in Finland and Netherlands, in many other countries we were able to gain market share in the advertising market. And I think that is a demonstration of the strength of our titles and brands and the capabilities that our teams have in the different parts of our company. And I think the only clear underperformance was in the kiosks, but that is to some degree explained by the change in the opening hours environment in Finland which led to lower customer volumes.

The Eastern markets, the international part of the Sanoma Media division is rebounding. Of course there's a way to go to the 2008 levels, but we're clearly seeing the economic improvement in Russian and with that the rebounding of the advertising market. And since the revenue share of advertising in Russia is much higher than they'll be having in some other markets, this is very important for our future revenue performance. Regarding the other Central Eastern European countries, the picture is somewhat less positive, but we believe that gradually we're getting back to a growth trajectory in most of the operating markets also in the Central and Eastern Europe, and longer term expect a growth to happen.

A really important change in our organisation took place beginning of this year. The TV and radio operations, the gaming operations of Sanoma Entertainment were combined with the Sanoma Magazines to form the Sanoma Media division. And this is in alignment with our fundamental belief that a local multimedia position is a position that Sanoma can benefit from also in the future. And starting from this year we will be working under this operating structure as you can see from the chart. But I think more important that the organisational chart is why we did it, and that again is to support the cross media development in the different markets that we operate.

A few words again on our focus going forward. There are two main themes that we have in here. The first one is organic growth, it's clear that the current growth rate is not satisfactory. We have pockets of organic growth in the media sector because of the digital transformation. There are areas of faster growth that we need to look into in more detail. We have some examples and pockets all over the company where we have substantial growth rates and we need to be able to take advantage of these opportunities in a more systematic way. And that will require to increase the co-operation in the company, but also being more active with external partners and customers. Innovation is naturally a key element of that. We have a vibrant innovation community in the company. Innovation takes place locally in many of our units, in all of our units, I would say, and that is something that we need to just get more focus on. We have prioritised some areas of innovation going forward and that is part of the programme for this year to substantially improve our ability to scale these innovations.

The other element is to focus the operations to meet the requirements of the digital transformation. And we will continue to capitalise on the Sanoma Media organisational change to build on our strong positions in many local markets. And in addition to that, continue – or as part of that – to continue to invest in the digital products and services which have developed very well during the last few years. And learning is a growth opportunity for us; the learning vertical is undergoing a fundamental change due to digitalisation and also because of the natural pressures in the market. And we think Sanoma is extremely well positioned to take advantage of these opportunities going forward.

Then a few words about the outlook for 2011. If we look at the net sales and operating profit in total, the guidance is that we expect those to be at the previous year's level. What I would like to point out here that the growth trajectory is on a comparable basis if you adjust for the structural changes is on roughly the same level as we've had before. So, no major change there. And then when you analyse the operating profit performance, I would like to point out the impact of the structural changes which is about €10 million due to Welho and Humo. And the assumption here is based on our ability to continuously protect our content revenues, i.e. to continue to compensate somewhat the challenges in the circulation and the subscription area part of the market is going to be reasonably flat, but then the single copy or the pressure on the single copy market, and an outlook on a future somewhat growing advertising market as a basis for this estimate.

Then about the dividend proposal of €1.1, a reminder that we have had the policy of stable dividends, a good dividend yield has been important to Sanoma. We have stated that we have – if you look at our actual dividend per share and compare it to our cash flow per share, you can see that that has been quite stable and consistent. The earnings per share has been more volatile given the impact of impairment and now this year the impact of the Welho divestment. And this year the proposal is based on this continued strong fundamental cash flow, an improved result and then the impact of the Welho transaction which motivates to us the somewhat higher dividend proposals for 2010.

With that I would thank you from my part and hand the word to Kim, and then after Kim's presentation we'll open up for questions. Thank you.

Kim Ignatius

Thank you Harri-Pekka and good morning everybody and a very warm welcome also on my behalf. My name is Kim Ignatius and I'm the CFO of Sanoma Group. Very pleased to be here today and walk through the 2010 financials as well as commenting the Q4 result for the company. We did have a strong full year. Our net sales were fairly stable compared to last year, and as mentioned adjusted to the group structural changes we grew during the year with 1.5% and during Q4 with roughly at 1%. What we are very pleased with is the profitability improvement which is a result of all the efficiency measures that we have taken during the last few years and which led to an EBIT improvement of 60 million or 7%. The performance in the last quarter was not as good as it was during the first three ones as some trends were changing, some patterns were changing and I will come back to those during the coming slides. Our earnings per share at the very good level, 185, impacted by the Welho transaction but also impacted by some of the write downs that we did during the latter half of the year. Cash flow developing positively and the number of employees continues to go down.

Looking at the quarterly performance, first of all I think that this picture always acts as a good reminder of the volatility that we have in our business between the quarters.

Secondly, what it shows, it shows the impact of the divested operations and also the increase marketing expenditure during Q4. What comes to the sales, the impact started to be visible at the latter half of the year, which you can see in this graph. For the profitability the structural changes really impacted more on the Q4 numbers, but even more so did the increased advertising and marketing spending. Our marketing spending for the full year increased by roughly 30 million, and of that increase 10 million took place during the last quarter. So, what that tells is that there was some cautiousness during the first half of the year in marketing spending having a fairly bad visibility to the market development. And now towards the end of the year we are returning closer to normal levels. The marketing spending levels in 2009 were at an exceptionally low level in Q4. What comes to the underlying performance of our different divisions in Q4, I could say that almost all of our operations did perform according to our expectations except for trade.

Just a few comments on the sales development, I think this is a good analysis for you to understand the changes during 2010, but also to understand how things are developing going forward now in 2011. Magazines flat sales, sales were negatively impacted by the sale of Humo in Belgium. On the positive side we have the improving advertising markets plus to some extent foreign exchange changes. In News, our sales development was very good both in print and in digital, and in addition to going with the markets we also did gain some market share. The number would be even better if you take into consideration the fact that Esmerk was transferred for part of the year to another division, plus that we sold Lehtikuva during the year. In Entertainment, we can clearly see the impact of the Welho transaction. Putting that aside the performance of Nelonen Media was very good actually for the full good the sales increased by 12% and for the last quarter even with a much higher growth rate. So, good performance in Nelonen Media. In Learning and Literature, the learning part of the business did very well, also some improvements in the other areas, mainly in the language services. For Trade, we see the impact still of the bad economic situation in the Baltic, but more so the changes in the sales makes customer volumes in the Finnish kiosk operations. When it comes to the profitability the sales decline is not the major challenge, but more so the sales mix.

Looking at our post days (?) operating expenditure, having flat sales being able to improve our EBIT, a big portion of that of course comes then from our operating expenses. The paper cost at the level of 150 million came down last year by close to 19 million. Also the other cost of goods sold developed positively being 12 million lower than the year before. Our employee benefit expenses came down by 27 million. So, these were the plusses where we did increase our spending as mentioned was in the advertising and marketing, and in the ICT development.

Looking at the EBIT on divisional level first, magazines a great performance in 2010 driven by the advertising markets developing positively, also having lower paper cost, lower printing cost, plus employee benefit expenses being better than the year before. Really the main improvement in the magazines P&L is in the gross margin level. News also performing very well, 6.6 million improvement coming from the improved advertising sales and lower paper costs. What is burdening the result of News is that reduced holiday payments in 2009 which was then offset by additional bonuses paid out in 2010. Taking this to include this in the picture the actual improvement in the performance would have been even much better. Entertainment, impact again from the divestment of Welho, but as you can see of the numbers the reduction in the EBIT doesn’t really show to the fullest, the impact of Welho disappearing. So, again Nelonen Media doing a very good job. In Learning and Literature, a good performance driven mainly by the learning business, to some extent to the other businesses as well as to lower overhead spending. Trade, again the same two things impacting the sales mix and the lower customer volumes.

In Q4 where we saw changing trends because of based on the reasons that we have walked through, in magazines really two things impacting the development. One is the structural change in Belgium selling Humo's operations and the other is increasing marketing spending in the Dutch markets. News, efficiency improvements and the continuous good development of both print and digital advertising. Entertainment, the same trend as we see in the impact of Welho and on the other hand the improved profitability of Nelonen Media. What comes to Learning and Literature, which is four million below last year, as mentioned by Harri-Pekka we have some write downs of operational ICT solutions on the level of two million. We did inventory adjustment plus we had lesser sales from our digital educational solutions in the Polish market. And this is a business that in 2009 had very high gross margin levels. So, this is impacting in learning's results for 2010. And Trade we have already commented. We did have some quite high non-recurring items in 2010, the biggest one being the sale of Welho at 179. Then we took a write-down or an impairment on the value of Aldipress, our press distribution operation which was transferred to the magazine division, and as mentioned in Q3, this was more of a technical IRS impact of transferring it to be a standalone cash generating unit instead of the global retail trade operations. We also did take down the value of Hansaprint. Hansaprint is an associated company for us, our ownership is 40%, the impairment was 22 million, and that is based on the estimated declining cash flows going forward with that operation.

Cash flow, which is more and more important also to understand how the businesses are developing, if we take our EBITDA, adjust that with our gains from the sales of Welho and other assets and take also into the picture the film and broadcasting rights, we see that our cash flow really from the operations improved by roughly 36 million. So, major improvement in the efficiency of our operations. Change in working capital, positive, a little bit less than last year, but still positive. And the interest paid during the year clearly lower than in 2009, this all leading to a very good level of 273 million for the full year. Our financial flexibility has strengthened during 2010; this comes from the improved profitability. Good focus on networking capital management and our capital structure is, as said, stronger than the year before, our equity ratio improving to a level of 45.6%, our net debt to EBITDA ratio for the time being, being as low as 1.5. These together with the strong positions that we have in the marketplaces gives us a good basis to develop our businesses forward.

This ends my part of the presentation and if I may I'd like Harri-Pekka to come back to the stage and we can take questions from the audience.

Harri-Pekka

Maybe you should stay here in case there are.

Questions and Answers

Teemu Vainio – Öhman

What do you expect on a group level the paper costs to be in 2011 as the paper press hikes have been announced?

What we're expecting is a development normalising it back to close to 2009 levels. So, we will probably see a double digit growth in paper costs. Just one comment, the number is in newsprint there, the total number will be less.

Sami Sarkamis – Nordea Markets

I have a question on your cost level in Q4; I think that came as a surprise to many analysts. Could you elaborate on how you were behaving differently in Q4 than in the previous quarters, and what should we assume as far as this year is concerned regarding your behaviour in terms of marketing expenditure and IT investments for example?

Kim Ignatius

Yes, as mentioned earlier we take the advertising and marketing expenditure. So, for the full year we increased our spending by 30 million of which 10 million took place in Q4. So, on the full year level the increase was only a bit over 10%, so not a drastic change. We were very careful during the first half of the year and then increasing towards the end. So, I don't think you should look at Q4 as a basis for the coming quarters, but more on the annual level understanding that 2009 was a very low marketing spending year. The ICT spending is volatile of course, you have projects, you develop your support ICT solutions plus operational, and they go up and down. So, again not a guidance for the full year next year where we were in Q4.

Harri-Pekka

I think maybe one comment on ICT on that, of course we will continue to invest in digital platform, for example, but we also seek to benefit from using similar infrastructure solutions to find also some of that investment from doing things together in a new way.

Then a follow up question on your guidance, I think that on the EBIT level it looks quite conservative and especially looking at divisions, the new Media division, News division and the Learning division, how come you don't assume an improvement even though the market conditions should improve? Are you assuming that the cost increases will offset this growth?

There are a couple of remarks I would like to make on that point. I think first of all I think you need to factor in the structural changes and the impact of those. The other one which is a factor in here is the paper cost development which goes against us this year. The advertising market is expected to improve, but in a way we receive part of that benefit on the latter part of the previous year. And then of course we as our companies want to continue improving our operations, but you have to have realistic… we expect it to be on the same level as before. It's hard to get a step change on that dimension.

Thank you.

Kim Ignatius

There are right now no other questions from the room, maybe we could take some questions over the phone and then come back to the room.

Mark Braley – Deutsche Bank, London

Good morning, two questions. First a technical one, could you tell us what the share of profit from DNA was during the part year that it was treated, or the part year that you had the associate holding so we can get an idea of what a full year of ownership might look like there? And then the second one is more forward looking, can you give us a feel for what you think an achievable organic revenue growth is for the business in normalised economic conditions, so a couple of years out as the strategy pays off, how should we think about top line growth?

Kim Ignatius

Starting with the DNA which of course now has only been half a year in our financials, and we take their share of the net profit in our associated company lines, and that was around ten million for last year.

Harri-Pekka

Regarding the organic growth, I think the historic growth of the media industry as such is one way to look at it, but at this point I don't want to give any guidance on what our organic growth target should be, that is something that we're working together with the team. But it is a focus that we need to look into very carefully to try to find ways to speed up the organic growth rate of the company.

Thank you.

Nicholas Kristofferson – Cheuvreux, Stockholm

Nicholas Kristofferson, thanks for taking my questions, I have two. And firstly Aldipress, just if you can remind us what was the EBIT result in 2010 so we're not lost in the translation of this unit back to the magazine. And then secondly, last year you had in your guidance allowing for investments in the magazine operation, now we have marketing investments seem to be returning to some sort of normality, is it fair to assume that you have less headroom in this year?

Kim Ignatius

If I start with the Aldipress question, we haven't published the EBIT levels of Aldipress, it has earlier been consolidated into the Trade numbers and now will be consolidated into the magazine division numbers, but the profitability has been close to break even. I guess if you're referring to the headroom for the marketing spending, my comments on guiding for this year during the quarters where we in the quarterly meetings made statements saying that we're preparing for a need to have an additional spending level towards the end of the year, this actually took place as we had earlier stated. I would go back to my earlier statement, as I said, that if you look at the full year spending levels that we have here and take into consideration that hopefully the markets are improving and more activity is needed. So, there isn't any specific buffers being built into our guidance, more now with the improved disability, the way we see things going forward.

Thank you.
Kim Ignatius

We can turn it back to the room here.

Sami Sarkamis – Nordea Markets

I have one question regarding your dividend proposal. I think you mentioned that the Welho divestment was one of the reasons for coming up with current dividend proposals, does it mean that if you look at the payout ratio out of the cash flow, are we on the high side for the time being or should we assume this level going forward?

Kim Ignatius

I think you have to first of all look at the trends from the past and how the relationship of the dividend payout has been with the earnings, but also with the cash flow and the capital structures. At any given year it's a combination of many many things. It's your financial performance, it's your capital structure, it's how you see your business is developing forward and what kind of investment needs you have. We have a stable policy, stable practice, but it's very difficult to say where we will be in the coming years.

Thank you.
Bengt Dahlström – Swedbank

Returning to your 2011 outlook, am I correct in assuming that you look at the advertising revenue growth for this year below last year when it grew by 8%, is that your assumption for this year?

Harri-Pekka

We expect advertising growth to continue. We know or we expect to see probably similar levels at the beginning of the year because of the baseline, the comparison of the beginning of last year is low. I think then we're prudent with regards to the rest of the year to be conservative here at this point because we don't have a crystal ball on that front.

What's your assumption on the advertising revenue development in Eastern Europe?

It is very market specific. We have seen good growth, for example, in Russia supported by the economic development. But then in many other countries it's lower, so you would have to go and break it down by market.

Thanks.

Kim Ignatius

If there are no additional questions maybe Harri-Pekka some closing remarks.

Closing Comments

Harri-Pekka

I would like to thank you all for your time and interest and I think it's time to conclude this presentation and meeting. Thank you all for your good questions and interest.