

Q1

2020



Restructuring measures start to have an impact, financial position improved and order backlog grew

This is not an interim report as specified in the IAS 34 standard. The company complies with half-yearly reporting according to the Finnish Securities Markets Act and discloses business reviews for the first three and nine month periods of the year, in which key information regarding the company's financial situation and development will be presented.

The financial information presented in this business review is unaudited. Figures in brackets refer to the corresponding period of the previous year, unless otherwise stated.

Financial development January–March 2020

GROUP	1–3/2020	1–3/2019	1–12/2019
Net sales, EUR million	119.4	117.8	667.7
Change in net sales, %	1.3%	14.2%	-7.5%
Operating result, EUR million	-3.5	-9.3	-41.8
Operating result, % of net sales	-3.0%	-7.9%	-6.3%
Result for the period, EUR million	-3.8	-7.6	-35.7
Order backlog at period end, EUR million	502.6	671.4	481.8
Earnings per share, EUR	-0.06	-0.13	-0.61
Cash and cash equivalents, EUR million	69.4	18.5	59.2
Interest-bearing liabilities, EUR million	183.8	240.3	189.2
Lease liabilities in interest-bearing liabilities, EUR million	57.0	99.2	46.8
Equity ratio, %	29.9%	28.9%	29.6%
Net gearing ratio, %	106.3%	158.1%	115.9%
Equity ratio, excl. IFRS 16 lease liabilities, %	35.5%	36.3%	33.8%
Net gearing ratio, excl. IFRS 16 lease liabilities, %	53.4%	87.4%	74.1%

First-quarter net sales, EUR 119.4 (117.8) million, remained in the same level as in with the corresponding period of the previous year. Net sales grew in the Housing service area and declined in the Business Premises and Social Care and Educational Premises service areas. The handover of two projects in the DWS portfolio contributed to net sales growth in Housing.

The operating loss was EUR 3.5 million (operating loss of EUR 9.3 million). The completion of the previous year's loss-making projects had a positive impact on the operating result. The result was still burdened by ongoing school projects with a weak margin, weaker profitability in Housing service area compared to comparison period as well as high fixed costs in relation to the volume of operations.

The balance sheet position developed favourably. Interest-bearing liabilities declined and cash and cash equivalents grew to EUR 69.4 million (EUR 59.2 million on 31 December 2019). The decline in net working capital in particular contributed to positive cash flow.

The order backlog rose to EUR 502.6 million (EUR 481.8 million on 31 December 2019). The order backlog increased in the Housing and Business Premises service areas, but declined in the Social Care and Educational Premises service area.

The current Social Care and Educational Premises service area was integrated into two other service areas effective 1 May 2020. Care home construction are handled by the Housing service area and the construction of schools by the Business Premises service area. In future, net sales will be reported for these two service areas.

NET SALES BY SERVICE AREA, EUR MILLION

	1-3/2020	1-3/2019	CHANGE	1-12/2019
Business Premises	36.4	39.6	-8.1%	170.8
Housing	71.9	63.1	13.8%	409.2
Social Care and Educational Premises	11.1	15.1	-26.1%	87.7
Total	119.4	117.8	1.3%	667.7

CEO Hannu Lehto:

"The year began on a good note. The restructuring measures we initiated last year are starting to have an effect and business is proceeding according to plans. Operations are now in better shape and projects are more firmly under control.

First-quarter net sales were at the previous year's level. Although the operating result saw significant year-on-year improvement, it was still negative. This was due to factors such as typically weak first quarter in the Housing business, the low profitability of school projects and high fixed costs in relation to the volume of operations.

We have scaled our operations and cost structure to correspond to the lower volume. During the first months of the year, we engaged in two employee cooperation negotiations that sought not only to adjust personnel resources to the operational volume, but also to prepare for the uncertainty caused by the coronavirus pandemic. As part of our measures to reduce fixed costs, the Group's Executive Board and the management teams of the service areas have voluntarily committed to lowering their earnings by 20 per cent for a five-month period.

We have merged the Social Care and Educational Premises service area into two other service areas. Care home construction will continue in the Housing service area and school construction in the Business Premises service area. Thanks to these actions, fixed costs are declining.

The coronavirus crisis that began in March ushered in new business challenges. In spite of the crisis, sales have gone well and our inflow of new work has outpaced the completion of projects. Our order backlog grew by slightly over EUR 20 million in the first quarter.

Customers are more cautious and new project startups are being delayed. Some projects have been cancelled and transactions pushed back to a later date. Demand for housing among consumers has slackened significantly, but institutional buyers remain active. On a positive note, the number of unsold Lehto housing units that are under construction or have been completed is relatively low.

The coronavirus crisis does not have an immediate impact on construction, as the projects are typically long in duration. As long as we work on projects and customers remain solvent, we will generate earnings and cash flow. We will now keep our focus on sales and project development to ensure that we are well poised to succeed going forward, too.

Our crisis awareness was at a good level even before the pandemic. We have now started up corrective actions and are relatively well equipped to tackle new challenges. Lehto's long-term objective is to transform construction and to engage in high-quality, reasonably priced, fast and ecological construction. We believe that there will be a particularly great need for reasonably priced construction in difficult times."

Outlook for 2020

In a stock exchange release published on 7 April 2020, Lehto withdrew its guidance on its 2020 financial outlook. The guidance was withdrawn because the coronavirus pandemic has created greater uncertainty in Lehto's business environment and the visibility has weakened.

So far Lehto's projects have progressed nearly without interruptions but starts of some new projects are delaying because of decisions made by the customers. The company sees risks related to sales, project execution and availability of materials, subcontracting resources and labour resources. Realization of the risks would have effects on Lehto's year 2020 net sales, profitability and financial position.

Lehto estimates that the new guidance could be given later this year.

Business development in the review period

At the end of the review period, Lehto completed employee cooperation negotiations, as a result of which it decided to merge the functions of the Social Care and Educational Premises service area into two other service areas. Care home construction will continue in the Housing service area and school construction in the Business Premises service area. However, this business review reports on the Social Care and Educational Premises service area in accordance with the earlier structure. As from the second quarter onwards, Lehto will report on only two service areas, Housing and Business Premises, and will present comparative information accordingly.

BUSINESS PREMISES

The net sales of the service area decreased by 8.1% year-on-year to EUR 36.4 (39.6) million. Four projects were completed during the review period, the largest of which was a commercial building in Vantaa. At the end of the review period, 17 projects were under construction, most notably three hotel projects in the Greater Helsinki area, a logistics centre in Kerava and a Prisma hypermarket in Varkaus.

Commercial performance was good in the first quarter. New contract agreements valued at EUR 44.3 million were signed during the period, increasing the order backlog to EUR 201.7 million (EUR 185.2 million on 31 December 2019).

Due to the coronavirus crisis, the start-up of a number of projects was delayed, and contract negotiations on some projects were halted. Projects started up before the crisis have progressed in line with plans and there have been no significant disruptions in their implementation.

Lehto has developed the Hippos2020 project with the City of Jyväskylä. Progress on the project is now more uncertain as a result of the coronavirus crisis. Lehto and the City of Jyväskylä are engaging in ongoing dialogue about the conditions necessary to continue with the project.

Complete renovation operations

Lehto's Building Renovation service area was discontinued at the beginning of 2019 and its ongoing projects were transferred to the Business Premises service area for completion. Its large loss-making projects were completed in late 2019.

The Business Premises service area still has two complete renovation projects to implement based on earlier commitments. One of the projects is a complete renovation contract valued at about EUR 27 million in which an old office property is being renovated and converted for use as a hotel. Work on the project is ongoing and it is progressing in line with plans. The other project is a contract valued at about EUR 14 million in which old teaching facilities will be renovated and converted for use as housing. The construction phase of this project is being started up and it is possible that the margin of the project will be slightly negative.

SOCIAL CARE AND EDUCATIONAL PREMISES

The net sales of the service area decreased by 26.1% year-on-year to EUR 11.1 (15.1) million. Care homes and assisted-living facilities accounted for EUR 3.4 (9.2) million of net sales, while schools and daycare centres accounted for EUR 7.7 (5.9) million. Four care homes and two daycare centres were completed during the review period. At the end of the review period, six schools and one daycare centre were under construction.

Demand for care homes remained low and no new care home projects were initiated. However, after the end of the review period, Lehto has signed agreements to build new care home projects. The company estimates that demand for care homes and assisted-living facilities will grow in the future.

In the school business, Lehto continued work on building ongoing projects. No new school projects were started up. However, Lehto has continued to offer new school projects and promote this business.

The order backlog of the Social Care and Educational Premises service area at the end of the review period was EUR 17.9 million (EUR 29.2 million on 31 December 2019). The decline in the order backlog is due to the decrease in the number of care sector properties in the backlog.

After the end of the review period and the merger of the Social Care and Educational Premises service area into other service areas, Ville Kettunen stepped down from the Lehto Group's Executive Board.

HOUSING

Net sales in the Housing service area grew by 13.8% from the comparison period to EUR 71.9 (63.1) million. The handover of two housing projects included in the German DWS housing portfolio in March contributed to net sales growth.

Sales of housing units went well during the review period and saw year-on-year growth; 210 of the sold units were related to the DWS portfolio.

SOLD HOUSING UNITS DURING THE REVIEW PERIOD

	1-3/2020	1-3/2019	1-12/2019
Contract	660	226	338
Developer contract	123	231	1,499
Sold housing units during the review period, total	783	457	1,837

During the review period, 428 (209) housing units were completed and the construction of 514 (490) new units was started up. About half of the units started up were in the Greater Helsinki area, half in the Turku and Tampere regions. One project was located in Rovaniemi. At the end of the review period, 1,481 units were under construction, which is at the same level as at with the turn of the year (1,485) but significantly lower than at the end of the comparison period (3,603).

HOUSING UNITS UNDER CONSTRUCTION

	1-3/2020	1-3/2019	1-12/2019
Under construction at the beginning of the period	1,485	3,322	3,322
+ started up during the period	514	490	1,035
- postponed project	-90		
- completed during the period	-428	-209	-2,872
Housing units under construction, total	1,481	3,603	1,485

The number of housing units completed or under construction declined further. This is due not only to the good trend in sales, but also the fact that the focus in housing projects has shifted from developer contracting to contract projects. In a contract, all the housing units are considered to have been sold at the time of signing.

UNSOLD HOUSING UNITS

	31 Mar 2020	31 Mar 2019	31 Dec 2019
Under construction	262	1,759	518
Completed	170	61	276
Unsold housing units, total	432	1,820	794
including DWS units	192	542	402

The order backlog of the Housing service area grew and amounted to EUR 283.0 million at the end of the review period (EUR 267.4 million on 31 December 2019). The housing production order backlog includes the proportion of started developer contracting projects that has not been recognised as net sales. A construction project is included in the order backlog once the decision to start construction has been made and the contract for a developer contracting project has been signed.

After the review period, a long project development phase was completed when the agreements for a housing complex project in Kalasatama, Helsinki were finalised. Lehto will build a complex of three housing companies in Kalasatama, comprising a total of five blocks of flats with more than 300 apartments as well as commercial premises.

The complex will also include a parking facility, which will be built under its yard deck. Two of the housing companies have been sold to institutional investors. Lehto will implement the third housing company as a consumer project.

Pipeline renovations

Pipeline renovations are carried out by Lehto's Housing service area. Pipeline renovation operations remained steady and five projects were completed during the review period and 11 were under progress at the end.

The construction sites have continued well, despite the state of emergency caused by the coronavirus. Remote connections have been utilized with the housing companies and the shareholders of the housing companies in the necessary contacts during the implementation of the projects.

The demand situation has also remained good, but there has been a delay in the decision-making of housing companies. The company sees that the need for pipeline renovations will continue to be steady in the future, and by utilizing remote connections, project decisions and communication with customers during projects can be handled in an efficient way.

SWEDISH OPERATIONS

During the review period, the focus of Swedish operations was on completing an ongoing daycare centre project and starting up the construction of wooden blocks of flats.

Lehto has developed a type of wooden block of flats based on prefabricated space elements. Lehto is currently negotiating with customers and financiers on the implementation of the first pilot project. In the first phase, it is intended that projects will be carried out as fixed-price contracts, with the construction phase being implemented with local partners.

Balance sheet and financing

CONSOLIDATED BALANCE SHEET, EUR MILLION

	31 Mar 2020	31 Mar 2019	31 Dec 2019
Non-current assets	56.5	48.5	55.8
Current assets			
Inventories, excluding IFRS 16 assets	196.2	294.1	210.3
Inventories, IFRS 16 assets	50.0	91.1	40.1
Current receivables	76.9	144.1	86.3
Cash and cash equivalents	69.4	18.5	59.2
Total assets	448.9	596.3	451.8
Equity	107.7	140.3	112.1
Financial liabilities	126.9	141.0	142.4
Lease liabilities	57.0	99.2	46.8
Advances received	88.5	110.9	73.2
Other payables	68.9	104.8	77.3
Total equity and liabilities	448.9	596.3	451.8

The balance sheet total remained at the same level as on the 2019 closing date. Inventories committed to projects decreased, particularly because two housing projects were handed over to DWS in March.

Cash and cash equivalents grew to EUR 69.4 million (EUR 59.2 million on 31 December 2019). The positive development of the cash position was affected above all by the EUR 29.3 million reduction in net working capital during the review period.

Funds released from net working capital were used to repay part of interest-bearing liabilities. Due to the decline in liabilities and increase in cash assets, interest-bearing net debt (excluding lease liabilities in accordance with IFRS 16) declined to EUR 57.5 million (EUR 122.6 million on 31 March 2019 and EUR 83.1 million on 31 December 2019).

At the end of the review period, the equity ratio, taking lease liabilities into consideration, amounted to 29.9% (29.6% on 31 December 2019) and the net gearing ratio to 106.3% (115.9% on 31 December 2019). The adjusted equity ratio (without the lease liabilities under IFRS 16) stood at 35.5% (33.8% on 31 December 2019) and the net gearing ratio was 53.4% (74.1%).

Lehto has a syndicated Revolving Credit Facility (RCF) of EUR 75 million with OP Corporate Bank plc, Nordea Bank plc and Swedbank Ab. The full amount of the RCF was lowered to EUR 54 million in 2019 and this amount was in use in its entirety at the end of the review period. The RCF is valid until November 2021 and is subject to standard covenants for profitability and indebtedness. The original covenant terms of the RCF were renegotiated during the review period and partial collateral has been given for it.

Personnel

The average number of personnel during the review period was 1,210 (1,557). The number of personnel at period end was 1,190 (1,274 on 31 December 2019); temporary layoffs amounted to about 27 person years. About half of the Group's personnel are salaried employees and half employees working at construction sites. On 20 February 2020, the company initiated employee cooperation negotiations as part of its restructuring programme. As a result of the negotiations, employees were terminated (69), laid off temporarily and transferred to other positions in the Group (29), with a total impact of 98 person years.

On 25 March 2020, Lehto started employee cooperation negotiations on potential temporary layoffs applying to all personnel. These negotiations were carried out due to the coronavirus pandemic, which is expected to have direct, indirect and possibly also long-term impacts on the business environment. According to the company's estimate, the changes caused by the pandemic might be related to delays in project start-ups and disruptions in the availability of materials and subcontracting resources. As a result of the negotiations, measures were initiated, mainly involving part-time layoffs. According to a preliminary estimate, the temporary layoffs will last until the end of the year.

The company has a long-term share-based incentive plan in place. The aim of the plan is to combine the objectives of the shareholders and the key employees in order to increase the value of the company in the long term and to commit key employees to the company. The plan is directed at a maximum of 70 key employees and the rewards are paid after a restriction period of two years, partly in the company's shares and partly in cash. The cash proportion is intended to cover taxes and tax-related costs arising from the reward.

On 26 March 2020, Lehto carried out a direct share issue related to the payment of the incentive for the 2017 earnings period of the share-based incentive plan. In the share issue, Lehto Group Plc transferred 50,341 company's own shares to 29 key employees of the Lehto Group in accordance with the terms of the incentive plan.

Repurchasing and transferring own shares

On 23 March 2020, the company commenced repurchasing the company's own shares to meet its obligations under the share-based incentive plans or for other purposes authorised by the Annual General Meeting. The share purchases ended on 2 April 2020 and the number of shares repurchased was 356,743 in total, corresponding to approximately 0.61% of the total number of Lehto's shares. The pecuniary amount used for the repurchase was EUR 500,000.

On 26 March 2020, the company transferred without consideration 50,341 Lehto Group Plc's own shares to key employees included in the incentive program in accordance with its terms and conditions. Information about launch the terms and conditions of the program is available in a stock exchange release was published on December 20, 2016.

On 4 May 2020, after the end of the review period, the company transferred without a consideration a total of 56,893 of its own shares to members of the Board of Directors in accordance with the decision taken by the Annual General Meeting and the voluntary reduction of Board remuneration announced on 29 April 2020.

The number of company shares is 58,309,558. After the repurchasing and transferring shares as part of the incentive plan and to reward Board members, the number of shares held by the company is 249,509.

Resolutions of the Annual General Meeting

In accordance with the proposal of the Board of Directors, the Annual General Meeting of 14 April 2020 decided that no dividend will be paid for the financial year ending on 31 December 2019.

The AGM confirmed the number of Board members to be five. Pursuant to the proposal made by the shareholders' nomination committee, Seppo Laine, Mikko Räsänen and Anne Korkiakoski were reelected as members of the Board of Directors, and Helena Säteri and Raimo Lehtiö were elected as new members. Martti Karppinen and Pertti Korhonen left the Board of Directors. The Board members' term of office will expire at the next Annual General Meeting.

At its organisation meeting, the Board of Directors decided to elect Seppo Laine as its Chairman and also decided to establish an Audit Committee. Anne Korkiakoski was elected as the Chairman and Mikko Räsänen and Seppo Laine as the members of this committee.

The above-mentioned and other decisions of the Annual General Meeting were disclosed in the stock exchange release of 14 April 2020.

Events after the review period

In a stock exchange release published on 7 April 2020, Lehto withdrew its guidance on its 2020 financial outlook. The guidance was withdrawn because the coronavirus pandemic has created greater uncertainty in Lehto's business environment and weakened visibility.

So far Lehto's projects have progressed nearly without interruptions but starts of some new projects are delaying because of decisions made by the customers. The company sees risks related to sales, project execution and availability of materials, subcontracting resources and labour resources. Realization of the risks would have effects on Lehto's year 2020 net sales, profitability and financial position.

Lehto estimates that the new guidance could be given later this year.

Lehto is prepared for the uncertainty and has completed co-operation negotiations on layoffs on all personnel. As a result of the negotiations, company will lay off its personnel according to the separate plans to be made in the service areas. According to the preliminary estimates, layoffs will last until the end of the year. In addition to personnel related measures, Lehto is planning and executing other cost-saving measures.

On 29 April 2020, Lehto announced that the Board of Directors will, at its own initiative, reduce its remuneration by 20 per cent from the amounts decided on by the AGM for a five-month period. The reduction in remuneration concerns both the cash and share components. By reducing its remuneration, the Board of Directors supports the profitability of the company and participates in the same saving measures as the company's management and operative personnel participates.

In addition, the CEO of Lehto Group Plc, the members of the Executive Board and the members of the management teams of the service areas have committed to lowering their earnings by 20 per cent for a five-month period. Significant part of Lehto's office employees are partly or fully temporarily laid off for approximately five months.

Vantaa 13 May 2020

Lehto Group Plc
Board of Directors

Further information:

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