EVLI

SRV

Construction & Engineering/Finland, March 31, 2020
Company report

Turning the ship in stormy waters

SRV's road has been bumpy in the past two years and measures are being taken to turn the tide. The slowing down of the Finnish construction market has created prerequisites for improved profitability by alleviating some supply chain pressure. The unfortunate Coronavirus outbreak casts a shadow over the planned turnaround and the uncertainty is reflected in valuation multiples. We adjust our target price to EUR 1.00 (1.30) and retain our HOLD-rating.

Seeking turnaround from recent weak profitability years

SRV's profitability has been in the red the past two years and the company is under new management seeking to turn the tide. Measures are being taken to enhance operational profitability and improve the financial situation. Market development has shown beneficial signs, as a slowing down of new construction volumes should ease supply chain pricing pressure. The Coronavirus outbreak, however, creates significant near-term uncertainty and any possible impact is yet hard to quantify.

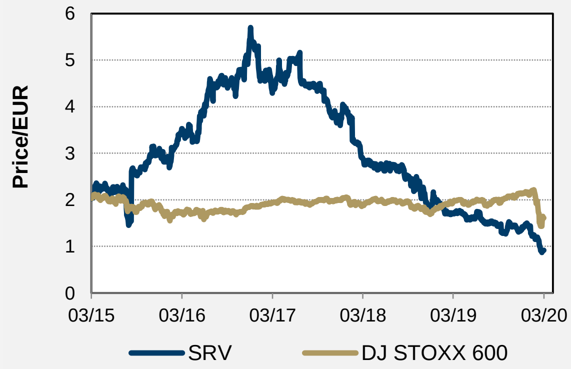
Volumes expected to decline, profitability improve

We expect sales to settle at a level of around 10% below the solid 2019 levels (EUR 1,060.9m) following an expected overall decline in construction volumes. 2020 remains supported by the lengthy order backlog while the completion of fewer developer-contracted housing units will lower sales. We expect profitability to improve in 2020 from the recent weak comparison years due to a diminishing burden of non-recurring items but margins to still remain relatively low. We estimate a 2020 operative operating profit margin of 1.1%.

HOLD with a target price of EUR 1.00 (1.30)

Our DCF and SOTP implied equity fair values are EUR 1.10 and 0.64 respectively. We derive a target price or EUR 1.00 (1.30) per share, assigning more weight to our DCF fair value due to an unjust near-term weight on profitability of our SOTP-model and retain our HOLD-rating.

Rating — HOLD



Share price, EUR (Last trading day's closing price)	0.92
Target price, EUR	1.0
Latest change in recommendation	18-Sep-18
Latest report on company	07-Feb-20
Research paid by issuer:	YES
No. of shares outstanding, '000's	59,581
No. of shares fully diluted, '000's	151,962
Market cap, EURm	55
Free float, %	33.2
Exchange rate	1.000
Reuters code	SRV1V.HE
Bloomberg code	SRV1V FH
Average daily volume, EURm	0.06
Next interim report	29-Apr-20
Web site	srv.fi/en/investors

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BUY HOLD SELL

KEY FIGURES

	Sales EURm	EBIT EURm	EBIT %	FCF EURm	EPS EUR	P/E (x)	EV/Sales (x)	EV/EBIT (x)	FCF yield %	DPS EUR
2018	959.9	-19.9	-2.1%	10.7	-0.57	-3.0	0.6	-30.2	10.6	0.00
2019	1,061.0	-93.1	-8.8%	-36.9	-1.80	-0.8	0.6	-6.3	-45.6	0.00
2020E	956.2	4.3	0.4%	78.2	-0.14	-6.7	0.5	101.3	142.7	0.00
2021E	966.1	19.9	2.1%	-26.3	-0.02	-40.6	0.5	23.1	-48.1	0.00
2022E	943.4	24.0	2.5%	70.8	0.00	-1,076.0	0.5	18.7	129.2	0.03

Market cap, EURm	55	Gearing 2020E, %	177.0	CAGR EPS 2019-22, %	-92.2
Net debt 2020E, EURm	379	Price/book 2020E	0.3	CAGR sales 2019-22, %	-3.8
Enterprise value, EURm	433	Dividend yield 2020E, %	0.0	ROE 2020E, %	-15.9
Total assets 2020E, EURm	917	Tax rate 2020E, %	20.0	ROCE 2020E, %	1.9
Goodwill 2020E, EURm	2	Equity ratio 2020E, %	23.6	PEG, P/E 20/CAGR	0.0

All the important disclosures can be found on the last pages of this report.

Investment summary

Finnish construction project developer

SRV is a Finnish project management contractor that develops and builds commercial and business premises, residential units as well as infrastructure and logistics projects. The company operates in Finland and Russia. In 2019 net sales amounted to EUR 1,061m and the company has around 1,000 employees.

Strong recent year market growth to slow down

The Finnish construction market has developed favourably in previous years and new construction volumes have seen large increases from earlier levels. Based on for instance housing unit start-ups in the near past, estimated to decline to 32,000 units by 2020 (2018: 45,600 units), construction volumes are however expected to decline to more normal levels in the coming years. The construction market slow-down has a two-fold implication, as although revenue will come down a more normal situation should alleviate supply chain pressures and discrepancies in profitability between constructors and suppliers/subcontractors.

Profitability has been challenging the previous years

SRV has during 2018-2019 seen profitability challenges, with two consecutive years of negative operating profit margins, relating mainly to its REDI Shopping centre project. 2019 saw operating profit margins in construction operations turn positive but significant amortizations kept earnings in the red. SRV expects full-year net sales for 2020 to decline compared to 2019 (EUR 1,060.9m). The operative operating profit is expected to improve and be positive (2019: EUR -96.8m). We expect sales in 2020 to decline mainly due to a lower completion of developer contracting units. We expect profitability to improve from the weak comparison period with the clearly smaller impact off one-offs and completion of certain weaker margin projects in 2019. Our 2020 sales and operative operating profit estimates are EUR 956.2m and 10.3m respectively.

Seeking measures to strengthen financial situation

The experienced profitability challenges have manifested in a weakened financial situation. SRV has taken a clearly more structured approach under renewed management and clearly strives towards creating a healthier business. In early 2020 SRV announced a series of measures to improve financial stability. These measures have led to the divestment of certain assets, at in our view generally unfavourable terms, but improved the more at-risk near-term cash flows. SRV will also seek to carry out two separate rights issues totaling EUR 141m. The first issue of EUR 91m is planned for conversion of SRV's hybrid loan + accrued interest while the second issue would constitute a rights issue of up to EUR 50m.

HOLD with a target price of EUR 1.00 (1.30)

We base our valuation mainly on our DCF-model and SOTP-approach, as on our estimates near-term profitability figures are expected to remain weak and high financial expenses keep earnings in the red. The value of balance sheet objects are in our view also better captured through the aforementioned approaches, when comparing with a peer-multiple approach. Our DCF and SOTP implied equity fair values are EUR 1.10 and 0.64 respectively. We derive a target price or EUR 1.00 (1.30) per share, assigning more weight to our DCF fair value due to an unjust near-term weight on profitability of our SOTP-model and retain our HOLD-rating.

The Coronavirus outbreak has caused significant uncertainty

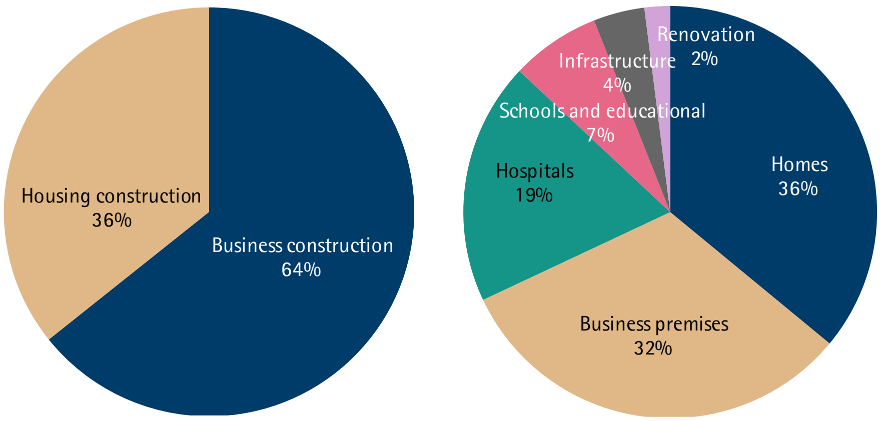
The on-going Coronavirus outbreak has caused significant near-term economic uncertainty. The construction sector exhibits a certain near-term resilience due to lengthy order backlogs and SRV has so far not noted any notable impact of the outbreak. Risks include work site impacts from potential quarantines and the availability of workforce, with measures having been taken to limit cross-border movement and a dependence on foreign labour, as well as potential supply chain issues. The economic uncertainty may also translate into a weakened housing market, with declining interest for new residential units and lower prices.

Company overview

Leading Finnish construction company

SRV is a Finnish project management contractor that develops and builds commercial and business premises, residential units as well as infrastructure and logistics projects. The company's construction operations are focused to Finland, while the company also is an investor in and operates several shopping centres in Russia. In 2019 net sales amounted to EUR 1,061m and the company has around 1,000 employees.

Figure 1: Construction -segment revenue split and revenue split per type, 2019



Source: SRV

Focus on project management

SRV's operating model is based on innovative project development and effective project management. In its projects, SRV is responsible for project management and specific tasks such as design and construction work are assigned to specialized subcontractors. SRV assumes responsibility for project completion according to price, time and quality requirements agreed with the client. SRV's subcontractor network encompasses some 4,000 companies.

Construction

Construction operations encompass both housing and business premises

SRV's construction operations include housing and business premises businesses. SRV develops and builds for instance housing, hospitals, retail premises, offices, logistics centres and hotels, as well as underground construction projects and other special premises for its customers.

The housing construction operations are mainly focused on Finnish growth centres, in particular the Helsinki metropolitan area. In 2019 SRV completed 808 developer-contracting housing units and had a total of 2,142 housing units under construction at the end of 2019.

Largest hospital builder in Finland

Hospital construction generated approximately 19 % of SRV's sales during 2019. At the end of 2019 SRV had two large on-going projects: Nova Hospital in Jyväskylä and HUS Siltasairaala in Helsinki and completed the TAYS Front Yard hospital project during 2019.

Investments

Manager of and investor in shopping centres

The Investments segment focuses on the management and realization of the Group's real estate investments. These include three shopping centers in Russia, two in St. Petersburg: Okhta Mall and Pearl Plaza, as well as 4Daily in Moscow. SRV divested its share of the REDI shopping centre in Helsinki during early 2020, a project constructed by SRV that was completed in 2018.

Strategy and long-term financial targets

Long-term financial targets focused on profitability

SRV's strategy and long-term financial targets were approved in February 2018. The targets were left largely unchanged from previous targets but the company left out its sales target. Following a phase of rapid growth the company's primary objective is to improve profitability. The targets are based on a continued moderate and steady financial growth in Finland and improvements in the Russian economy and growth in the company's developer-contracting business. The company has set its targets to be achieved in 2022.

Table 1: SRV's financial objectives

	Measure	Target 2022	Status 2019
Profitability	Operative operating profit margin	8.0%*	-9.1%
Profitability	Return on equity	At least 15%	-50.6%
Profitability	Return on investment	At least 12%	-15.2%
Balance sheet	Equity ratio	Over 35%	21.2%/26.4%**
Dividend	Payout ratio	30-50%, taking into account capital needs	0.0%

Source: SRV, Evli Research
*The operative operating profit margin of construction will rise to 8%. Of this objective, 6% will arise from construction margin and 2% from shopping centre rental income as part of associated company holdings.
**Excl. IFRS 16

Growth in developer-contracted projects targeted

According to SRV, the achievement of these strategic objectives will be based on moderate but steady economic growth in Finland, and Russia's economy stabilizing at a slightly stronger level. Growth in SRV's developer-contracted projects is also required. SRV seeks to divest shopping centers that are in the management phase when the market situation allows. In order to achieve profitability targets, SRV will seek to boost the efficiency of the company's own operations, as well as implementing a more prudent selection of new projects with regard to profitability and capital commitment.

Reaching targets will pose a challenge

SRV fell well short of all targets in 2019 mainly due to impairments relating to the divestment of SRV's ownership in the REDI Shopping centre, noting however that the targets are set for 2022. Nonetheless the targets are quite ambitious given that SRV has during the past decade failed to reach operating profit margins of over 5% and profitability has in the past few years been declining. Reaching the targeted profitability would in our view essentially require SRV's operations running faultlessly and an increased share of developer-contracting projects. Also, a continued economic growth as well as a healthier situation in the Finnish construction market would be necessary. In the past few years the sector has been pressed by the boom in construction, which has had a notable impact on SRV due to its reliance on subcontractors, as the boom saw increased subcontractor pricing power and reduced overall subcontractor quality, as well as a limited availability of skilled workforce. With the divestments of the REDI Shopping centre, we expect that SRV will seek to lower its operative operating profit margin target, as SRV will no longer be entitled to the associated rental income.

SRV's guidance for 2020

Expect lower sales and clearly improved profitability in 2020

SRV expects its full-year consolidated revenue for 2020 to fall compared with 2019 (revenue in 2019: EUR 1,060.9m). The operative operating profit is expected to improve and be positive (operative operating profit in 2019: EUR -96.8m). Measures to boost operational efficiency and achieve savings in procurement are expected to improve the company's earnings performance. In addition, the recovery programme measures that were carried out in late 2019 are expected to improve the company' cost structure.

586 developer-contracting housing unit completions expected in 2020

SRV expects fewer developer-contracted housing units to be completed in 2020 than in the comparison period. It is estimated that a total of 586 developer-contracted housing units will be completed in 2020 (808 in 2019).

Financial performance

2019 a second year of profitability challenges

SRV's revenue grew by 11% in 2019 and amounted to EUR 1,060.9m (959.7m). The revenue growth was to a larger extent attributable to housing construction, where the number of developer-contracting housing units recognized as income increased from 2018 by 282 units to 808 units. The business construction revenue also grew, by 2.0% in 2019, contributing slightly to the growth in Group revenue. The group operative operating profit[1] declined to EUR -96.8m (-10.0m), representing a margin of -9.1% (-1.0%). Profitability was heavily affected by impairments relating to the REDI shopping centre divestment, amounting to EUR 71.5m. Other impairments in the investments segment during 2019, relating to the reclassification of Pearl Plaza as an asset held for sale and other impairments of plots and properties (mainly in Russia) amounted to EUR 17.7m. Within Construction, weaker margins in two projects had an effect on profitability of EUR -11.0m. Expense entries relating to water damage at the REDI Majakka housing project further affected profitability by EUR -6.0m and sales losses and impairments on plots by EUR -9.4m. The total impact of the aforementioned items on 2019 operative operating profit amounted to over EUR 100m. The operating profit decreased to EUR -93.0m (-19.8m), with a slight positive effect from a stronger ruble, with the total FX impact amounting to EUR -3.8m. The operating profit excluding impairments would have amounted to EUR 3.5m in 2019.

Improved suppliers' negotiation power has had an inverse effect on profits

Due to the good activity in the construction market in Finland, subcontractors and construction material producers have increased their prices. This has had a negative impact on profitability in the construction sector and especially on SRV as the company uses a large subcontractor network to execute projects.

Clear order backlog decline in 2019 following meager order intake

The order book at the end of 2019 decreased to EUR 1,344.2m (1,816.0m), with the sold share of the order backlog also declining to 81.4 per cent (2018: 88.7 per cent). The order intake was quite weak during 2019, with new orders of EUR 487.6m (2018: 1,133.0m). Significant new orders included for instance the second REDI tower: REDI Loisto, the Finnish-Russian school in Helsinki, the Wallesmanni and Opaali projects in Tampere, the Raisio production facility, the Siltasaari 10 renovation and modernization project, and the Kirkkonummi wellbeing centre.

High quarterly variation in result

According to SRV, variation in the Group's operating profit and operating profit margin is affected by several factors. A main operational factor is the developer-contracted projects being recognized as income upon delivery, while the lower-margin contracting projects are recognized as income based on the level of completion.

[1] Operative operating profit = operating excl. FX impact

Construction market outlook

Construction sector seeing volume declines after several boom years

The outlook for the Finnish construction sector has remained at reasonably healthy levels. The construction sector in Finland has experienced a strong boom in recent years and indicators are now pointing towards volumes declining towards a more normalized but above average level. According to the Confederation of Finnish Construction Industries RT, the Finnish construction market grew by 2.4% in 2018. In 2019 the market is expected to have declined 1.0% and in 2020 a further decline of 3.0% is expected. The deceleration is driven by slower growth in new construction, infrastructure, and housing production. Furthermore, construction of commercial and business premises is declining to a historically low level mainly because of a lack of new major projects compared to those completed during previous years. On the other hand, industrial construction and renovation construction is picking up significantly this year, the latter in particular picking up as the volumes of new construction is slowing down and subcontractor pricing and availability conditions are improving.

Volume in housing start-ups remain above decade average despite slowdown

Housing start-ups in Finland peaked at 45,600 units in 2018 and increased 2.5% compared to 2017 (44,500). The number is expected to go down to 32,000 units by 2020, but still sits slightly above the decade average (~30,000 units). The drop is due to a reduction in the number of non-subsidized apartment buildings.

Housing production has mainly focused on small apartment units

The average apartment size has fallen to 40 square meters in several cities. This can be explained by the fact that housing production has been strongly focused on small apartment buildings in recent years while detached and terraced start-ups have slightly decreased. As such, the completion of a larger share of smaller apartments has translated into a somewhat lower growth in volumes compared to the growth in housing units.

The number of granted building permits has been declining since 2017 peak

The decreasing number of building permits further suggests a slowdown in housing production. In 2018, building permits were granted for a total of 43,600 dwellings, which was 11.2% per cent fewer than in 2017 according to data from Statistics Finland. In 2019 granted building permits further declined by 14.3% to 37,400. In 2020, construction of detached houses and terraced houses are expected to decline slightly from 2018 levels, with apartment buildings start-ups expected to fall some 13,000 units below the peak in 2018 (34,400 units).

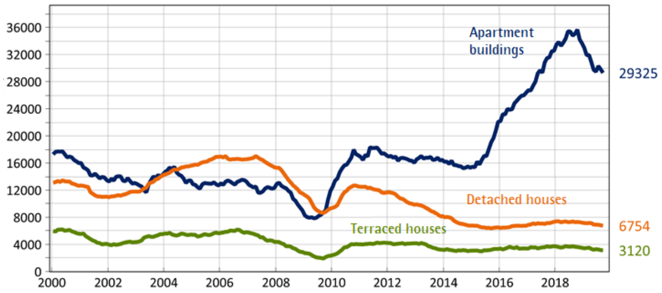
Coronavirus outbreak poses a threat to the otherwise reasonably good demand situation

Forecasts for growth in the Finnish economy have lately mainly been seeing downward revisions, although growth is still expected. In its February 2020 update the European Commission forecasted a 1.5% and 1.0% y/y growth in 2020 and 2021 respectively. We note that the Coronavirus outbreak will cause downward pressure to the forecasts and several financial institutions have forecast GDP declines in 2020. So far, the debt capital markets have provided market players with low financing costs. The Finnish housing market has been attractive under the low interest rate environment and higher yields in Finnish real estate landscape have translated into a solid foreign investor demand. In their market outlooks both RT and Catella anticipated another strong transaction year in retail markets. The growth outlook has previously given support for continued demand in the consumer housing market, but the economic impact of the Coronavirus outbreak poses a clear threat to near-term demand.

Lowered consumer confidence in comparison to recent years

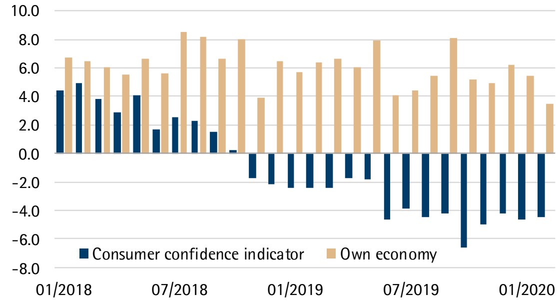
Consumers' optimism in the Finnish economy's strength has dimmed. In February 2020, according to Statistics Finland, the consumer confidence indicator stood at -4.5 (2/2019: -2.4) from worsened expectations regarding Finland's economy and employment. The Finns view on their personal economy has also declined slightly from levels seen in the past 12 months, decreasing to 3.5 (12m avg. 5.6) in February 2020. Early March 2020 figures show clearly weaker expectations regarding the Finnish economy but are not fully reflective of the more severe government actions to curb the economic impact of the virus outbreak.

Figure 2: Housing start-ups, variable annual sum



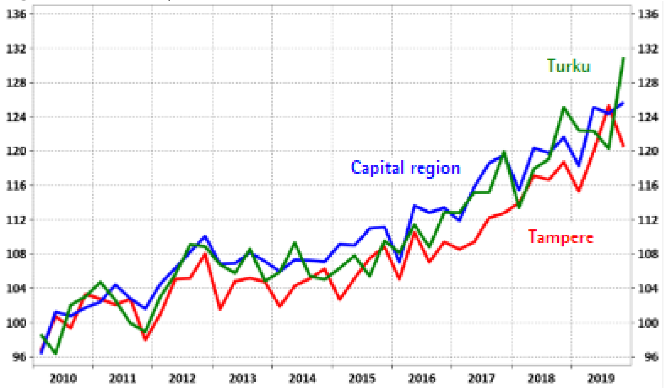
Source: Macrobond, RT

Figure 3: Consumer confidence, 1/2018-2/2020



Source: Statistics Finland, Evli Research

Figure 4: House price index for main Finnish cities, 2010=100



Source: Hypo, Macrobond

Housing prices have been on the rise only in major cities

Housing prices fell last year in all other growth centers except in the capital area, Tampere, Turku and Porvoo. Construction of new housing in these areas has been intense, which has somewhat eased housing shortages and kept prices in control. Demand is currently most concentrated to the central Helsinki area, where the increased housing construction has reduced housing availability deficits, but migration is keeping up demand. As shown in Figure 7 (Statistics Finland), housing prices of old dwellings deviated among the biggest 15 cities from -5.1% (Vaasa) to 2.5% (Helsinki). The corresponding figures for the second biggest gainers Tampere and Turku were 2.3% and 1.8%, respectively. Conversely, housing prices declined on the right tail of the sample. In 2018, the average house prices increased by approximately 0.6% (Statistics Finland). Based on preliminary from Statistics Finland the trend has continued during 2019, with housing price increases in Helsinki, Tampere and Turku driving figures for the country as a whole to slightly positive. SRV's largest housing projects are in Helsinki, Espoo, Tampere, Vantaa, Oulu, Turku and Jyväskylä, the seven largest cities in Finland.

Housing prices at national level expected to decline in 2021

Hypo estimates that, on a national level, housing prices will increase by 0.3% in 2020 and decline by 0.5% in 2021. Housing price increases have mostly been kept afloat by the capital region. Prices are expected to decline in 2021 following smaller price increases in the capital region, where Hypo predicts prices to continue rising by 1.5% in 2020, and 1.0% in 2021.

Population growth shifting towards large cities

A Growing number of people are moving to cities, and the reasoning is more than just work-related. Inevitably, better services and appealing "city lifestyle", as stated in Hypo's housing market review, could also be key criteria for migration. Nonetheless, the 14 largest urban areas currently account for about 74% of Finland's GDP and 72% of all jobs (KTI, 2019). Population was reported to decline in 247 municipalities in 2018, with only 27 cities showing clear growth. Figure 6 depicts the population change in the 15 largest cities in 2018.

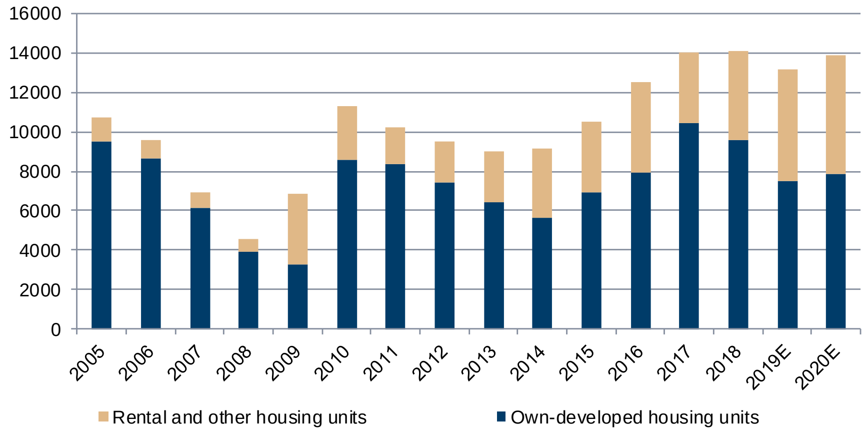
The Finnish population is aging, decreasing and moving to big cities

Nonetheless, given that urbanization and decelerating population growth continue to be prominent trends in Finland also in the forthcoming years, the housing market outlook will remain challenging at national level. Included in the shortlist in 2019 were Kajaani, Kotka, Kouvola, Mikkeli, Pori and Salo, for instance. This seems problematic for a number of reasons, most notably as prices in these areas may drop fiercely and cause over-indebtedness to citizens, whose properties do not sell even in a sluggish economy. According to the latest forecasts (Statistics Finland), the Finnish population is expected to increase on average by 0.1% p.a. until 2035, after which it will decrease and by 2050, the total population will have fallen below the present number.

Growth expected to be strong in the Helsinki area

Additionally, the population of Helsinki was estimated at ~650,000 inhabitants in the beginning of 2019, which was 7,000 more than a year before. The increase in population during 2018 was similar to that recorded during 2017. Within the next 25 years, the number of inhabitants in the Helsinki metropolitan area is projected to increase by 20-25%. (Statistics Finland)

Figure 5: Non-subsidized terraced and apartment housing starts, 2005-2020E

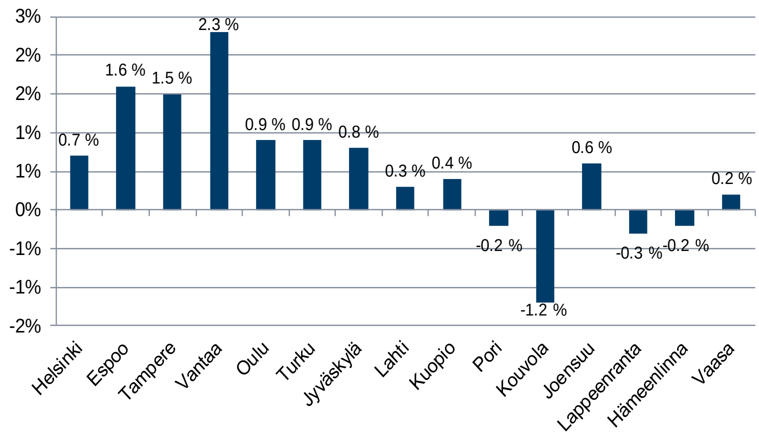


Source: Confederation of Finnish Construction Industries RT, Evli Research

Non-subsidized residential development start-ups expected to grow slightly

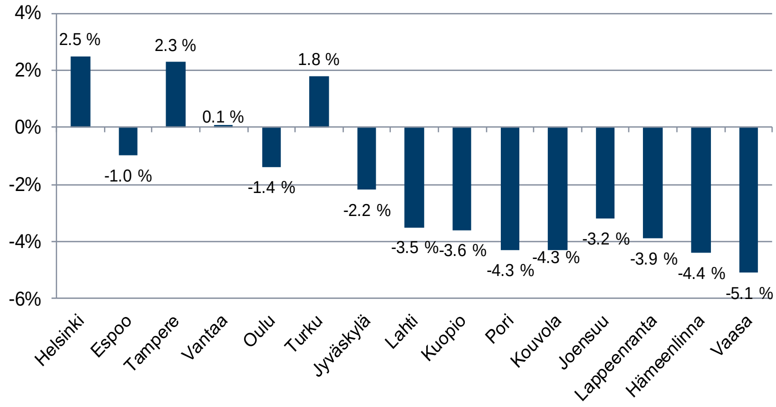
Non-subsidized residential development start-ups are expected to shrink clearly from 9,577 units in 2018 to 7,514 units (-21.5%) in 2019E. Rental and other housing start-ups, in contrast, are expected to increase by 25.0% to 5,670 units in 2019E, with the total decline in units expected to amount to around some 6.6% in 2019.

Figure 6: Population changes in 15 largest cities, % (2018)



Source: Statistics Finland, Evli Research

Figure 7: Housing price changes, % (old dwellings, 2018)

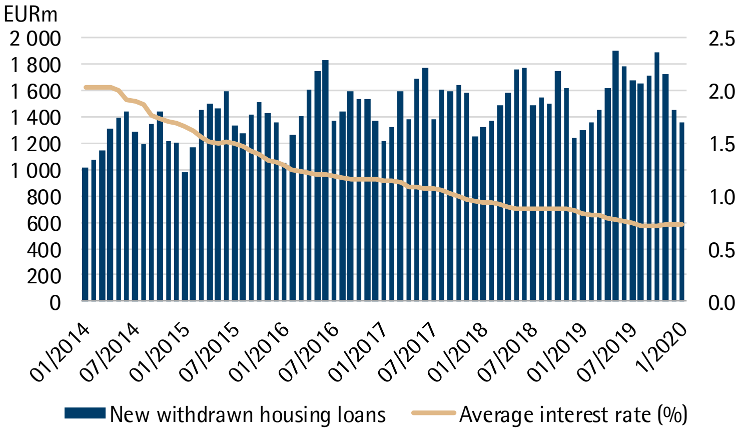


Source: Statistics Finland, Evli Research

Euribor rates remain negative

The average interest rates on new housing loans withdrawn hovers at just above 0.7%. The average interest rates have been steadily declining while the amount of withdrawn loans (annual average) has seen steady increases, up some 25% in the past five years. The Central bank changed its interest rate policy towards a slightly looser direction in the previous year. ECB previously signaled the key interest rate to remain at or below its current level, at least until mid-2020. Consequently, Euribor rates continue to stay negative providing convenience for mortgage holders.

Figure 8: Development of new housing loans withdrawn



Source: Bank of Finland, Evli Research

Property funds free capital from construction companies' balance sheet

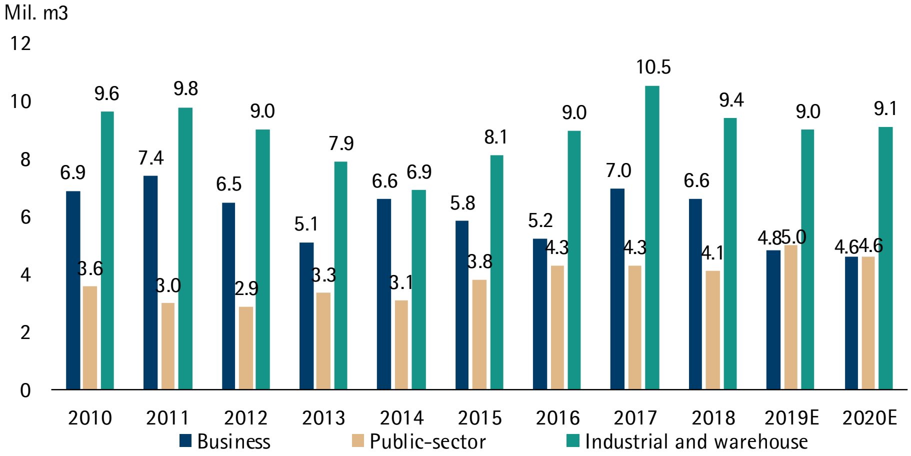
In the recent years, property funds investing in lease land lots have seen advances in the large cities. This somewhat new setting in the Finnish market frees capital from construction companies' balance sheet. The property funds have previously co-operated more with smaller construction firms but as of recently also with larger construction companies. Among others at least Hypo, Ålandsbanken, Taaleri, FIM and OP operate in the property funds market.

Non-housing start-ups projected to keep declining

Non-residential start-ups fell to 25.8 mil. m^3 in 2018. RT believes that the number will decrease further to below 24 mil. m^3 by 2020. The largest reduction will occur in business (commercial & office) construction, where RT expects start-ups volumes to dwindle as low as 4.6 mil. m^3 in 2020 from 2017 levels of 7.0 mil. m^3. The amount can be argued to be very low, as the corresponding levels of below 5.0 mil. m^3 were last seen in 1997. This can be explained by the fact that a large number of commercial projects were completed in previous years and there are few comparable ventures underway. For the same reason, traffic construction also decreases.

Industrial construction is instead expected to pick-up amid several notable projects in the battery, forest and marine industries. Industrial construction start-ups totaled 4.1 mil. m^3 last year and RT anticipates construction to grow by near 1 mil. m^3 in 2019 and exceed an aggregate of 5.5 mil. m^3 by 2020. Warehouse construction is declining despite supportive long-term trends from growth in online retail. Public sector construction is still at a record level and is expected to remain at high levels in the near-term. Recent developments in the public sector construction have been mostly due to the aging population, older buildings, and urbanization.

Figure 9: Non-housing start-ups development by category



Source: Statistics Finland, RT estimates, Evli Research

Outlook for renovation construction improving with decreases in new construction volumes

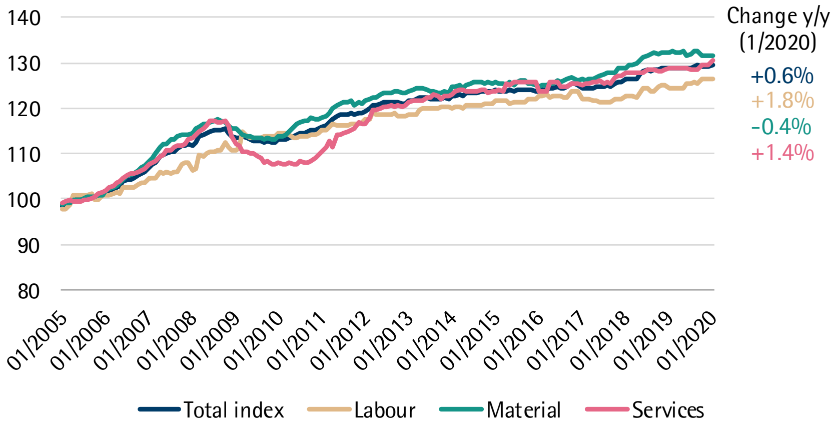
The upswing in construction in recent years has favored especially the construction of new housing premises, while the renovation construction saw a slight decline in growth. With the new construction showing signs of slowing down in the coming years, renovation construction is set to continue on a steady growth track. According to RT, renovation growth will continue to grow at near 2% in the following couple of years. The main factors for growth are the high age of the Finnish building stock and the renovation debt accrued over the years. A decrease in new construction volume will alleviate subcontracting challenges faced by renovation companies during the construction boom and likely also increase construction companies' exposure towards renovation construction.

Construction costs

Construction cost increases slowed down in 2019

The growth in construction costs slower down in 2019, after an increase of 2.4% in 2018, driven by the strong development in construction volumes. The previous years have seen strong demand especially in residential construction, which in turn has increased producers' capacity utilization rates and accordingly led manufacturers to increase their margins. The total cost index showed a clearly slower increase of 0.6% y/y in January 2020, with construction labour showing the largest increase at 1.8%. Material costs have leveled of and declined y/y after having shown rapid growth beginning in 2017.

Figure 10: Construction cost index, 2005=100

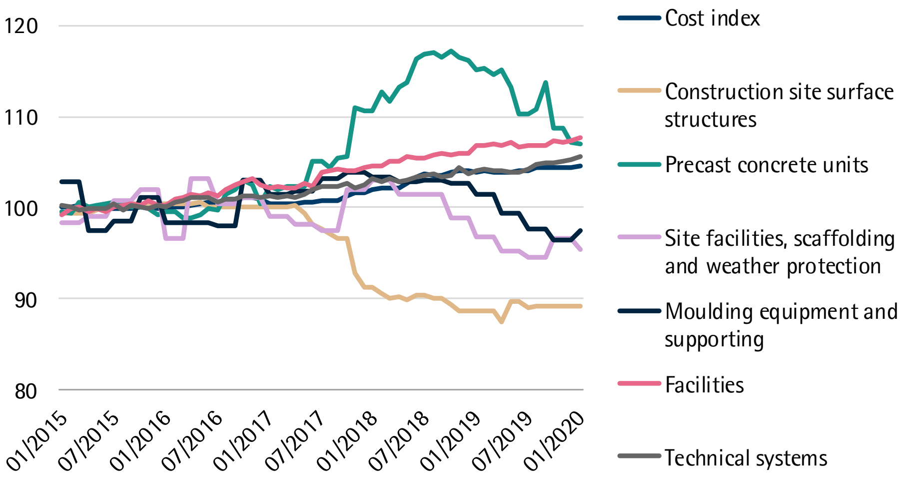


Source: Statistics Finland, Evli Research

Development of early stage construction costs supports overall slower cost development

The continued increase in construction costs in 2019 has largely reflected the continued large on-going construction volumes, despite construction start-ups having shown signs of decreases. When viewing the development of construction costs by input type, some indication is given of the nature of the cost development. Costs arising from earlier stages of the construction projects, such as precast concrete units and earlier stage equipment and structures have been showing declines largely throughout 2019 and 2020, while later stage cost inputs such as interior structures and facilities and technical systems have still been increasing. Although analysis based solely on the statistics is at a rather rudimentary level, the development in our view supports a view of continued overall slower cost development and potential further declines in the coming years.

Figure 11: Selected changes in construction costs in Finland, 2015=100



Source: Statistics Finland, Evli Research

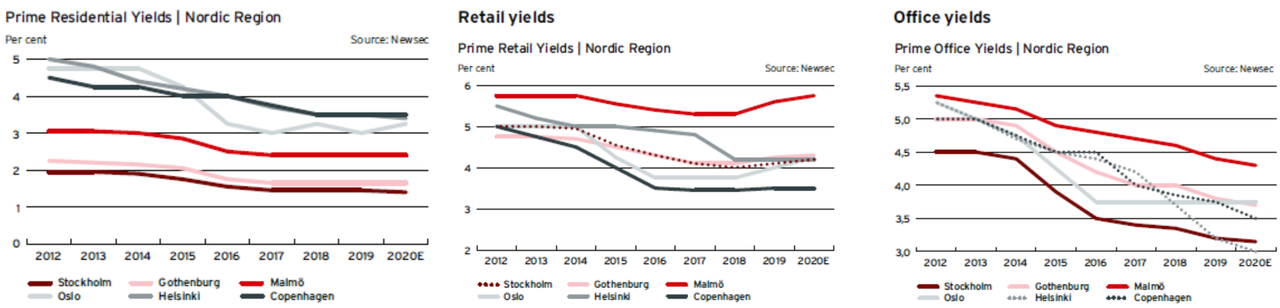
Yields

Investor' real estate demand declined in 2019

The Finnish property investment market saw strong demand in 2018, with Helsinki having been the strongest candidate among investors. The modern city center, good location and attractive rents kept foreign investor' appetite high. As a result, yields on the best properties have narrowed close to the prices of Europe's largest markets and starting to resemble those in Stockholm's according to Newsec. Other urban centers, such as Turku and Tampere, have as a likely result seen an increasing number of international investors arriving on the scene. 2019 saw a slight change in the overall situation, with the total real estate volumes in Finland falling to 6.3bn compared with the around 10bn levels seen in 2017-2018, driven by a disparity in supply and demand. The real estate sector remains an attractive investment sector but with scarcer supply the volumes will likely remain at lower levels.

The graphs in figure 12 show the development of prime residential, retail, and office yields in the largest Nordic cities between 2012 and 2020E (Newsec). The yields have decreased concurrently since 2015 due to improved investor demand. Prime retail yields in Helsinki plummeted to 4.3% in 2017 but have since remained relatively stable. Completion of the Mall of Tripla shopping centre in 2019 has in part increased the retail competition and increased pressure to lower rents. Helsinki prime office yields have declined clearly in recent years and are now among the lowest in the Nordics, with demand for offices having remained strong and rents being at record high levels.

Figure 12: Prime residential, retail, and office yields in the largest Nordic cities



Source: Newsec

Business model

Focus on project management

SRV's operating model is based on innovative project development and effective project management. In its projects, SRV is responsible for project management and specific tasks such as design and construction work are assigned to specialized subcontractors. SRV assumes responsibility for project completion according to price, time and quality requirements agreed with the client. The main competitive edges are strong project management skills and efficient implementation of the projects.

Commercial and business premises

SRV is responsible for project completion according to price, time and quality. According to SRV, commercial and business premises construction are typical areas in which the company's business model brings the greatest benefits. The company's project management model is competitive especially in large scale projects.

Own project development units

The company's target is to increase the share of revenue accounted for by its own development projects. SRV has its own project development units in Finland and Russia that are responsible for land acquisition, concept design and finding investors and anchor tenants. Own development projects have clearly higher profitability compared to competitive contracting.

Residential development business offering higher margins

SRV is also a major residential developer especially in the Helsinki region. In the residential development business, SRV acquires plots, takes responsibility of the design and establishes housing corporations. The company owns plots in the growth centers next to good transport connections. To our understanding, residential development business offers the highest margins in the business portfolio.

Takes part also in infra projects

In infra projects, SRV also operates in the role of main contractor. However, many infrastructure projects come ready planned, zoned and financed, which limits potential for value creation. These projects are typically carried out at fixed price.

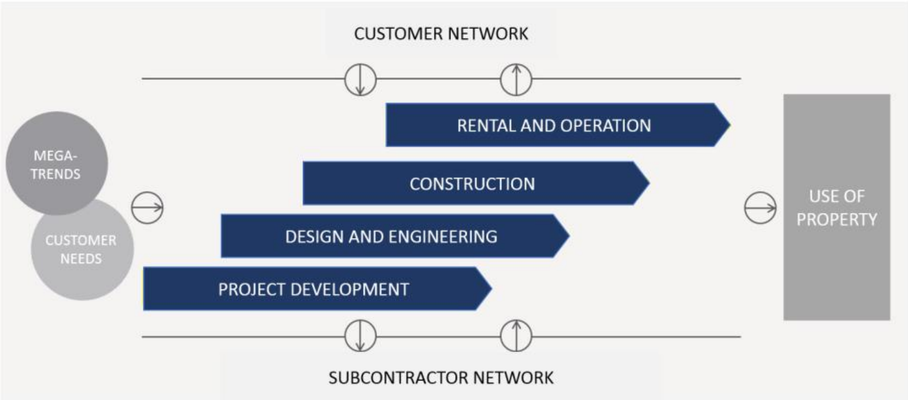
Residential development business offering higher margins

SRV's business model is relatively scalable compared especially to other listed Nordic construction companies. The company uses a large subcontractor network (~4,000 companies) annually. This enables SRV to undertake several large-scale projects at the same time. During economic downturns, the company can scale down its operations more quickly. In addition, during an economic downturn subcontractors pricing power is typically weak. During an upturn, subcontractors have more pricing power as they can be more selective with projects.

Own development projects increase risks

Increasing the share of own development projects also increases risks. In the own development projects, SRV bears the risks involved in both sale and construction of such projects. In addition, high share of own development projects typically lowers the return on capital ratios.

Figure 13: SRV's operating model



Source: SRV, Evli Research

Cost structure[2]

High share of variable costs due to operating model

SRV has a network of approximately 4,000 subcontractors. Consequently, the company's variable costs are significantly higher compared to many listed Nordic construction companies. The ten-year average variable costs share of net sales has been at 87.5%. In 2019, the share of variable costs was slightly above the 10-year average at 91.4%, affected in part by the suboptimal operational performance. In addition, prices of building materials have been at elevated levels.

Share of fixed costs has decreased

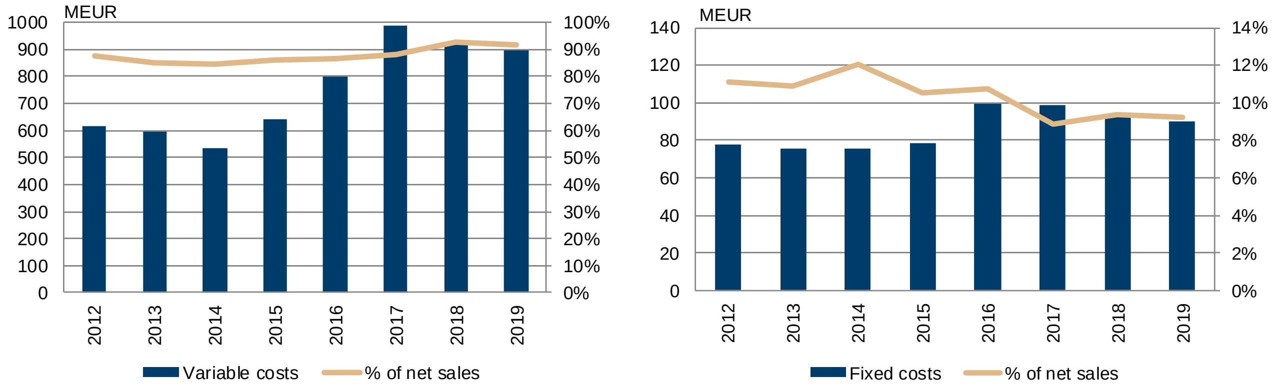
Due to the operating model focusing on project management, SRV's fixed costs are relatively low. The company has in recent years been able to slightly reduce the share of fixed costs of net sales, which however did not translate to earnings improvements due to the increases in variable costs. In 2019, fixed costs represented 9.2% of the net sales, while the ten-year average is at 10.6%. The number of SRV's own personnel has remained relatively steady during the past years.

Ability to adjust cost structure

Due to the high share of variable costs, SRV can adjust its operations to meet lower demand relatively quickly. For example, in 2014, when the construction market fell by 3.6% the company was able to reduce its variable costs both absolutely and relatively.

[2] Variable and fixed costs Evli Research' interpretation, figures not reported by SRV. Share of net sales adjusted for changes in works in progress

Figure 14: SRV's cost structure. Variable costs (left) and fixed costs (right)



Source: SRV, Evli Research

Construction segment

The Construction segment covers all of SRV's construction activities in Finland and Russia and includes the capital and plots required for developer-contracted housing production. Construction encompasses housing construction, business construction, technical units and procurement, and internal services.

Housing construction

SRV operates mainly in large Finnish growth centres

SRV constructs housing units both as own developer-contracted units and as units sold to investors. SRV's largest housing projects are in the large Finnish cities of Helsinki, Espoo, Vantaa, Tampere, Oulu, Turku and Jyväskylä. The company is one of the largest housing constructors in the Helsinki Metropolitan Area. Approximately 60% of the net sales were generated by developer-contracted projects and 40% by other housing construction in 2019. SRV has during several years on average been able to increase its developer-contracted business.

Sales growth 30.7% in 2019 due to more developer-contracting housing unit completions

SRV's housing construction sales declined in 2018 to EUR 288.4m, down by 24% compared to the previous year. The decline was largely due to the decrease in own-based housing completions. In 2018, SRV recognized 523 (825) own-based housing units as income, with a total recognized income of EUR 122m (2017: EUR 209m). The average housing unit price was at EUR 233k compared to EUR 254k in the previous year. In 2019 the housing construction sales picked up and grew 30.7% y/y to EUR 377.9m. The increase in sales was driven by the higher number of developer-contracted housing units recognized as income, with 809 units generating revenue of EUR 225.4m. The average housing unit price picked up to EUR 279k compared to EUR 233k in the previous year.

Start-ups picked up in 2019 after a significant decline in 2018

SRV's developer-contracting housing unit start-ups decreased by some 70% in 2018 to 317 units, after a peak year in 2017. Start-ups picked up clearly in 2019, with 780 new units. The start-up of REDI Loisto contributed to the start-ups with 249 units. The start-ups have mainly focused on the capital city region. As part of its strategy SRV focuses on building housing units in growing cities and in the vicinity of good transport connections. We note that with an average construction time of around 18 months, developer-contracting housing units are typically recognized as revenue in the second year after start-up. The company's developer-contracting projects under construction amounted to 835 units (2018: 863) at the end of 2019. Start-ups experience high cyclicality and single projects can have a significant impact on start-ups during a given time period. SRV's unsold completed developer contracting units amounted to 87 units at the end of 2019, which is a fairly low level. SRV has given guidance for an expected completion of 586 developer-contracting housing units in 2020.

2,142 housing units under construction

Currently, SRV has 2,142 (2018: 2,759) housing units under construction, mostly in the Helsinki Metropolitan area and other growth centers in Finland. Of the total housing units under construction, some 40% were in developer-contracting housing projects. Of the developer-contracting housing units under construction 56% were unsold at the end of 2019.

SRV carries out housing projects based on three project models:

Contract type	Construction project	Revenue recognition	Risk profile	Profitability
1) Developer-contracted housing project	Incl. plot acquisition, design, construction and final sale	Recognised when houses completed and sold	High-risk	EBIT-% typically above 10 %*
2) Development project	Incl. plot acquisition, design and construction – project sold to an investor before the start	Percentage of completion	Medium-risk	EBIT-% 5-10%*
3) Contracted project	Launched by others - constructed by the company	Percentage of completion	Low-risk	EBIT-% Below 5%*

*Evli estimate

Source: SRV, Evli Research

Business construction

Business construction accounted for nearly 65% of group revenue in 2019

In Business construction, SRV focuses on retail, office, hospital, school and logistics construction as well as earthworks and specialized rock construction. The business premises construction accounted for nearly 65% of total group revenue in 2019. Construction of hospitals accounted for 19% and business premises for 32% of group revenue respectively.

Hospital projects have been and important driver of sales

SRV's business construction sales grew by 2.0% and amounted to EUR 679.7m (666.2m) in 2019. Major completed projects in 2019 include the TAYS Front Yard for the Tampere University Hospital and several school projects. SRV is currently one of the leading hospital constructors in Finland.

Alliance projects offering possibility of higher margins

SRV also has ongoing alliance projects that have accounted for a smaller share of group revenue. In alliance projects SRV's margins are "above the ordinary level". In these projects, SRV has an opportunity to cooperate with a client in the design phase and lower risks in the project. SRV can also impact on the target price of the project. If the project is completed for less than target price and/or the project is completed prior to the deadline, SRV can gain additional earnings. A large on-going alliance project is the expansion of Terminal 2 at the Helsinki-Vantaa airport.

Order intake weakened during 2019

The order book decreased by 30.1% and amounted to EUR 861.5m (1,233.3m) at the end of 2019. SRV signed several large projects in 2018, for instance the Bridge Hospital project and Tampere Central Deck and Arena project as well as the Helsinki-Vantaa T2 expansion recorded in the order backlog in late 2018, and new deals signed in 2019 were clearly smaller.

Own construction equipment unit sold to Ramirent in late 2018

SRV used to have a construction equipment unit serving its construction business in Finland, SRV Kalusto, which was sold to Ramirent Finland in late 2018. The company owns e.g. site units, scaffolding, boring rigs, tower cranes and pile drivers. In conjunction with the divestment SRV signed a long-term with Ramirent covering a significant portion of SRV's equipment rental. SRV typically rents lifts and other equipment needed at sites.

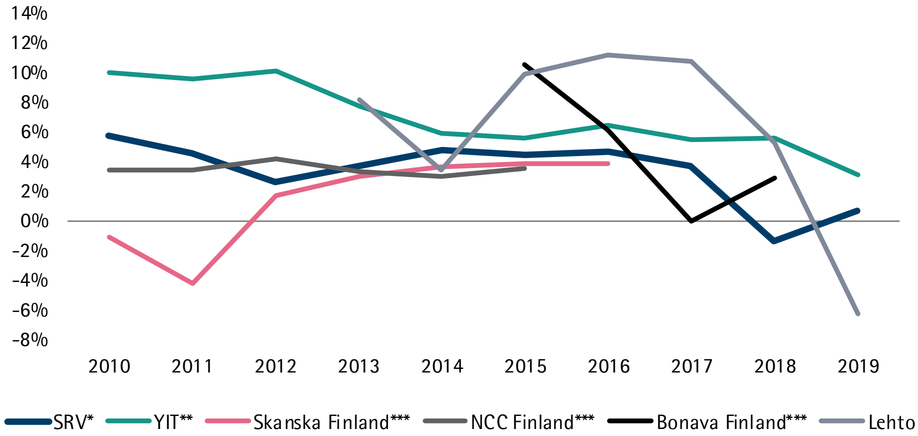
Competitor analysis

SRV's margins weakened against competitors

The following graph demonstrates the profitability of operations among SRV's main publicly listed competitors. We note that figures do not fully represent solely Finnish operations and reporting of Finnish figures has been dropped by several competitors. EBIT margins have seen fluctuations but in general remained at around 5% over the last 10-year period. Against this figure, SRV's EBIT has been 3.3% on average.

2018-2019 saw increased profitability challenges in the Finnish construction market. The impact was clearly visible for Lehto and SRV. Bonava has not reported figures for Finland in 2019 but saw weakened profitability and restructuring take place in 2019. Lehto has succeeded in achieving high profitability in earlier years but 2018-2019 saw profitability suffering from increased costs of unprofitable operations, especially in the renovation sector. For YIT we have included the Housing Finland & CEE, Business premises and Infrastructure segments, with the combined profitability seeing a decline from the previous year mainly due to Business premises, where profitability was affected by increased costs relating to a large shopping centre and two other projects.

Figure 15: EBIT margin development of main competitors in Finland



Source: Company financial statements, Evli Research

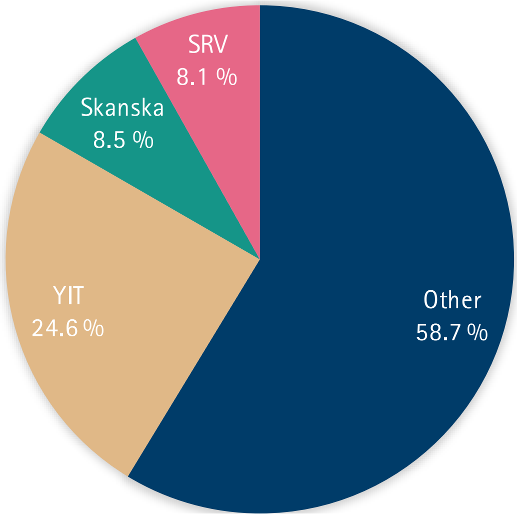
*Construction segment 2018-2019, **2014-2019 YIT Housing Finland & CEE + Business Premises & Infra, 2008-2013 Construction Services Finland, ***Skanska ended reporting of Finnish operations profitability externally in 2017 and NCC in 2016

YIT a clear market leader

Based on 2019 housing start-ups for consumers, SRV's market share was 8.1%. YIT is the clear market leader in Finland, with a market share of roughly a quarter. Skanska holds an estimated market share of 8.5%. Bonava held a share of slightly below 10% in 2018 but has not reported figures for 2019. Other large residential developers in the Finnish market are Lehto, Pohjola Rakennus, Lujatalo, Fira and Hartela along with several smaller players.

Profitability has been challenging, weak ruble has had a detrimental effect

Figure 16: Own-developed housing start-ups for consumers in Finland 2019E



Source: Company reports, Evli Research. Total developer start-ups from RT estimates.

Investments segment

Management of Group's real estate investments

The Investments segment focuses on the management and realization of the Group's real estate investments. The key objectives are to increase SRV's financing capacity through joint financing structures, creating added value through longer-term ownership, diversifying capital risk, and to generate positive cash flow. SRV's investment strategy revolves around the Group's strategy of building urban centres and harnessing the key megatrends that are affecting the built environment.

Co-investor in and manager of three completed shopping centres

SRV manages and acts as co-investor in three shopping centers in Russia, two in St. Petersburg: Okhta Mall and Pearl Plaza, as well as one in Moscow, 4Daily. In Finland the Investments segment managed the REDI shopping centre and parking lot that were opened in September 2018 but were divested during February 2020.

Revenue not an important metric due to booking of profits from associated companies

In 2018, net sales from International operations amounted to EUR 4.6m. Revenue consists mainly of revenue from shopping centre management. Revenue in 2019 grew to EUR 5.9m, supported by the startup of shopping centre management at REDI. As SRV owns shopping centers through its associated companies and joint ventures, their revenue is not presented in SRV's consolidated revenue.

The operative operating profit in 2019 amounted to EUR -96.3m compared with EUR -7.8m in 2018. The Investments segments profitability operatively has been burdened by high management and financing expenses from the recently opened shopping centers. During the construction phase, interest expenses are capitalized but once a shopping center is completed interest expenses are presented in full in the result of the company that owns the property. The operative operating profit in 2019 was exceptionally weak due to impairments totaling EUR 89.2m. Of these impairments' EUR 71.5m related to the REDI Shopping centre, which was divested in early 2020. The re-classification of Pearl Plaza as an asset held for sale had a negative effect of EUR 6.9m. Other impairments related mainly to properties and plots in Russia. The operating profit amounted to EUR -92.5m, alleviated slightly by a positive impact of the strengthened ruble.

SRV's international operations have during several years suffered from the weakening ruble. This has caused a major negative impact on SRV's profits from its Russian operations as ruble denominated revenues have declined. The historical weakening of the ruble has mostly been driven by lower oil prices. 2019 saw a strengthening of the ruble and as such an improved operating profit compared to the operative operating profit. In March 2020 the ruble saw a drastic weakening after a collapse of the OPEC+ production agreement.

Figure 17: EUR/RUB rates from January 2008 to present

Source: Bank of Finland, Evli Research

Investigating sale of Pearl Plaza

SRV is investigating the possible sale of the Pearl Plaza shopping center. SRV targets to divest its properties some 3-4 years from opening. SRV has now owned 50% of the Pearl Plaza shopping center over 5 years and the project has achieved a stable rental income level. SRV has held negotiations for divesting Pearl Plaza and signed a cooperation agreement with Sberbank Asset Management JSC Fund for a potential sale of the property. Pearl Plaza was re-classified as an asset held for sale in 2019. SRV is unlikely to divest Okhta Mall or 4Daily in the near future. Okhta Mall was opened in August 2016 and 4Daily in April 2017 and exits would likely take place around 2021-2022. The REDI Shopping centre and parking lot were opened in 2018 and divested in early 2020.

Ramp up of rental income takes years

During the first few years, shopping centres rental income in Russia is typically impacted by discounts, changing of tenants and relatively weak occupancy ratio. The low rental income is not sufficient to cover all fixed costs and financial expenses, which impacts on the result of associated company holdings. After the ramp-up period, the result improves significantly when target rental income level is achieved.

40% of SRV's invested capital

The Investments segments capital employed amounted to EUR 245.7m at the end of 2019, accounting for approximately 40% of the company's invested capital. Okhta Mall is the single largest property tying up capital, at EUR 88.6m.

Figure 18: Capital employed in the Investments segment

	31.12.2019	31.12.2018
REDI shopping centre and parking facility	24.6	118.4
Okhta mall, shopping centre	88.6	78.4
Pearl Plaza, shopping centre	25.3	25.3
Tampere Central Deck and Arena	25.8	13.8
4Daily, shopping centre	7.0	10.9
Plots to be developed and other holdings	74.4	91.0
Total	245.7	337.8

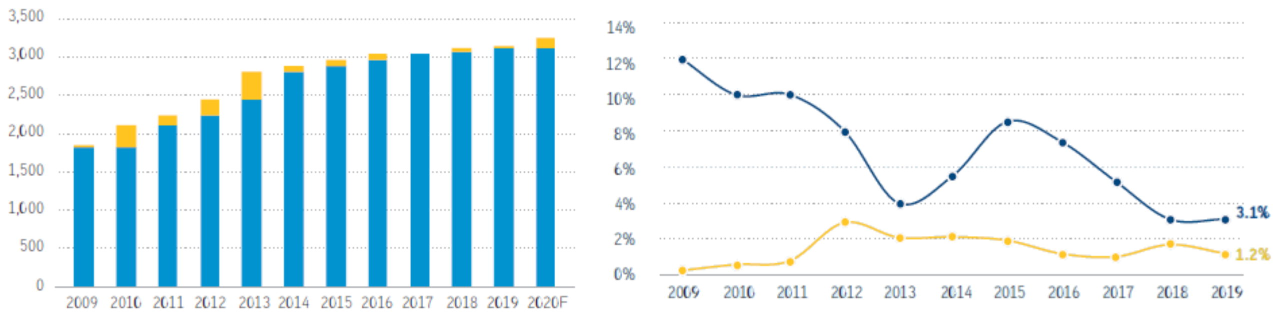
Source: SRV, Evli Research

Market conditions in the Russian shopping center market

Retail vacancy rates at 3.1% in St. Petersburg

In St. Petersburg, retail activity has seen good development. The average vacancy rate in the retail market remained near previous year levels and was 3.1% in 2019, according to Colliers market research. According to Colliers, an increase in quality renovations is a key trend within the shopping centres as growth in retail space has been limited. The shortage of vacant premises has led to increased competition for high quality spaces and high-class shopping centre owners being prepared to rotate tenants with an increase in rental rates. Colliers sees St. Petersburg retail yields in 2019 at 9-9.5%.

Figure 19: St. Petersburg increases in retail space, sqm thousands (left) and vacancy rates (right)

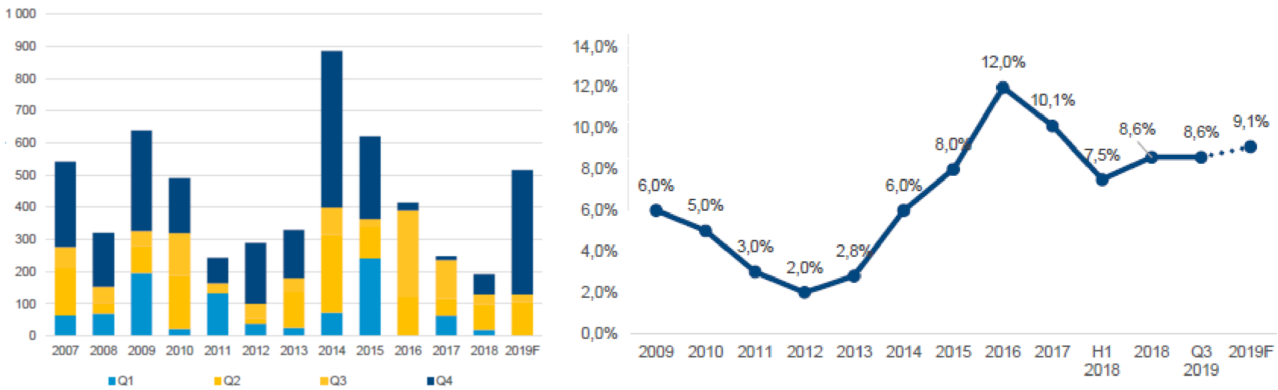


Source: Colliers International

Retail completions in Moscow expected to increase significantly in 2019 and vacancy rates to follow suite

In the Moscow region, vacancy rates in the retail market have decreased from the peak of 12% in 2016 but are seen to increase during 2019 to 9.1% following the introduction of large new projects, according to Colliers. The new retail completions in Moscow and its satellites have decreased rapidly after the peak in 2014, with H1/2019 completions of 105,000m^2 41% lower than the 10-year average. Retail completions are expected to have picked up during H2/2019 due to the completion of multiple projects and 2019 completions by GLA could amount to some 560,000m^2. Colliers sees Moscow retail yields in 2019 at 9-9.5%.

Figure 20: Moscow and satellite cities shopping centers completions, sqm thousands (left) and Moscow vacancy dynamics (right)



Source: Colliers International

SRV has stakes in three shopping centres

SRV has stakes in three shopping centers in Russia. In table 2, we have included key figures from the shopping centre projects. All the large property development projects in Russia are finished and no new projects have been initialized. The next significant stage for these buildings is their divestment. SRV has given some indicative times for exit timetables. However, these exit times cannot be taken as a certain as the development of the Russian economy and willingness of buyers clearly has an impact on the process. Nonetheless, we estimate some exit price ranges for these projects using the average Russian retail yields of 9% to 10%.

Table 2: Key facts of SRV's shopping centres

Project	SRV's ownership	Status	Leasable area (square metres)	Assumed net rental level (Evli)	Occupancy ratio %	Potential exit price*	Balance sheet value**	Exit time
Pearl Plaza, shopping center, St. Petersburg	50%	Opened in 8/2013	48,000	EUR 12m	100%	-	EUR 25.3m	2020
Okhta Mall, shopping center, St. Petersburg	45% + 15%	Opened in 8/2016	78,000	EUR 24m	97%	EUR 240-270m	-	2020-2022
4Daily, shopping center, Moscow	18.7%	Opened in 4/2017	25,000	EUR 7.5m	80%	EUR 75-85m	-	2020-2022

Source: SRV, Evli research estimates. * Exit range determined using 9-10% exit yield and assumed annual net rental level, **Pearl Plaza classified as asset held for sale in 2019

Financial position

SRV will continue its efforts to improve the balance sheet structure

In its recent financial targets, SRV has taken the initiative to improve balance sheet structure and liquidity. The strategy includes a more efficient circulation of working capital, implementing successful divestments and pay more attention to the projects in regard to their profitability and capital commitment.

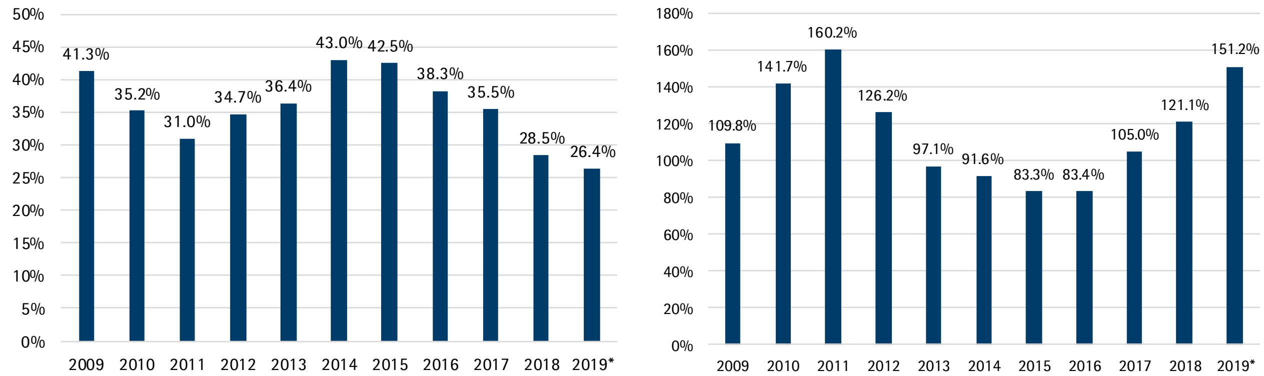
In 2018, SRV released more than EUR 90m tied capital through improvements in working capital and carrying out several divestments. This included, for instance, a sale of SRV Kalusto Oy to Ramirent Finland for EUR 21m. During 2019, SRV issued a new hybrid bond worth EUR 58.4m at a coupon of 12%. It enabled SRV to strengthen its balance sheet by paying off some of its current debt while increasing the proportion of equity. Of the proceeds, EUR 20.5m were employed for early repayment of the existing 8.750% hybrid loan and EUR 37.9m for early repayment of March 2021, 6.875% notes. In addition, SRV prolonged its current long-term binding revolving credit facility of 100 MEUR by one year, which together with the loan restructuring brought comfort to the loan portfolio maturities. The total hybrid loan sums to EUR 82.9m and comprises about 47% of total equity at the end 2019.

SRV's aim is to keep its equity ratio above 35%. The equity ratio at the end of 2019 without the impact of IFRS 16 was 26.4% compared with 28.5% in the comparison period. Net gearing amounted to 151.2% at the end of 2019 compared with 121.1% at the end of 2018. Taking into account the IFRS 16 imposed changes in treatment of right-of-use assets, the net interest-bearing liabilities increased to EUR 422.0m at the end of 2019 from EUR 282.2m in 2018. The most significant impact in this occasion stems from SRV's land lease agreements. Cash and cash equivalents totaled EUR 27.7m at the end of 2019, declining from EUR 93.1m at the end of 2018.

High invested capital due to property ownership

SRV's property development business and co-ownership in shopping center projects tie capital for a long period of time. At the end of the 2019, the invested capital in the Investments segment amounted to EUR 245.7m, corresponding to 40% of the total invested capital. This consists mainly of shopping center projects in Russia that SRV intends to sell in the next few years. First up is Pearl Plaza, which was expected to be divested in 2019, but will now likely be divested in 2020, with committed capital of EUR 25.3m. As a result, the transactions would provide SRV with flexibility through freed capital in the future. Capital employed in the Construction segment amounted to EUR 372.9m, representing some 60% of the invested capital at the end of 2019. Return on investment in the Construction and Investments segments at the yearend 2019 were at 3.0% and -32.6%, respectively.

Figure 21: SRV's equity ratio (left) and gearing ratio (right) development from 2009 to 2019



Source: SRV, Evli Research *excl. IFRS 16 impact

Measures to strengthen financial position

Series of measures announced in Q4/2019 to strengthen the financial position

SRV announced a series of measures in conjunction with its Q4/19 report to improve its financial situation. SRV has agreed to sell its ownership in the REDI shopping centre as well as part of its ownership in the Tampere Deck and Arena -project. SRV is further planning two separate rights issues and making changes to its revolving credit facility.

Sold REDI shopping centre ownership and part of Tampere Deck and Arena -project

SRV sold its 40% stake in the REDI shopping centre in February 2020. As a result, an EUR 71.5m impairment charge was recorded in Q4/2019w. The sale includes and earn-out and the final purchase price will be determined when the property is divested by the new owners within seven years. The near-term cash flow impact will be some EUR 21m, including the purchase price and certain receivables. SRV recorded a EUR 13.5m earn-out, of the EUR 50m maximum. SRV has further sold part of its ownership in the Tampere Deck and Arena project (remaining share after divestment approx. 8.33%) and Ranta-Tampella apartment project. The near-term cash flow impact will be some EUR 23m. SRV will further be released from EUR 15m investment commitments.

Two separate rights issues

Two separate rights issues have been agreed upon, totaling approx. EUR 141m. The first would be a directed share issue corresponding to the nominal amount of the hybrid notes and accrued interest, approx. EUR 91m, and would be offered to hybrid note holders in order to convert the hybrid notes into shares. Commitments have so far been received for approx. EUR 57m in principal and accrued interest. The commitments have been issued with a subscription price of EUR 1.05 per share. The second share issue would be a rights issue of up to EUR 50m. SRV has received commitments amounting to EUR 40m.

Amendments to SRV's revolving credit facility

SRV entered into a facility agreement regarding the conversion of its existing EUR 100m revolving credit facility into two separate revolving credit facilities of EUR 60m and EUR 40m.

Impact of planned measures

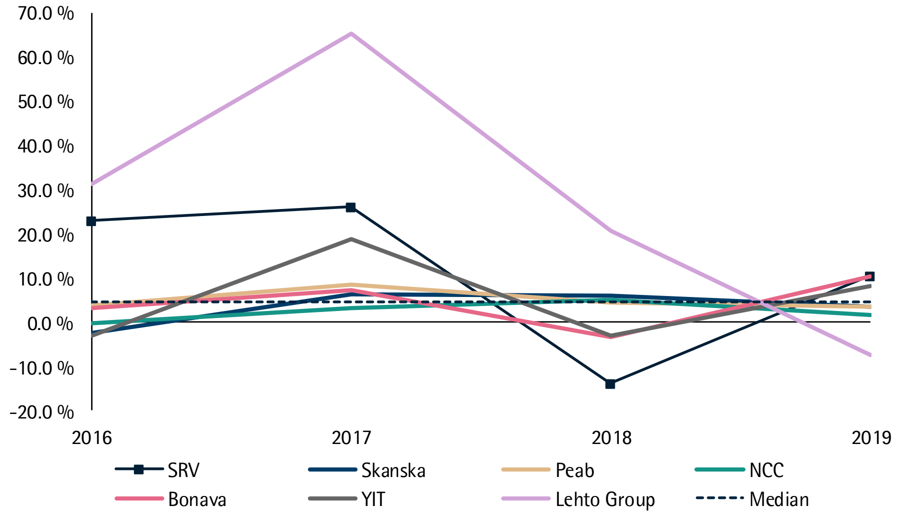
If the intended measures are carried out as planned, SRV's equity ratio will improve to a level of approximately 35 to 38 per cent and its net gearing (without the effect of IFRS 16) will improve to approximately 75 to 85 per cent. The cash-flow effect of the contemplated actions, if materialized, will be positive by approximately EUR 95 million (approx. 45m from sales proceeds and 50m second rights issue).

Peer comparison

EBIT margin has not kept up with revenue growth

SRV experienced healthy growth years during the start of the construction boom in 2016 and 2017, growing 22.9% and 26.0% respectively. In 2018 revenue took a hit following overall sales declines in both business and housing construction, with net sales falling 13.9% to EUR 959.7m in 2018, while simultaneously experiencing a larger decline in profitability due to additional costs in the REDI shopping centre project, with the operating profit margin at -2.1% in 2018. 2019 saw revenue return back to growth with the completion of a larger number of developer-contracted housing units, while profitability was heavily affected by impairments. Figures 22 and 23 illustrate SRV's development compared to its main Nordic peers.

Figure 22: Revenue growth of SRV and competitors

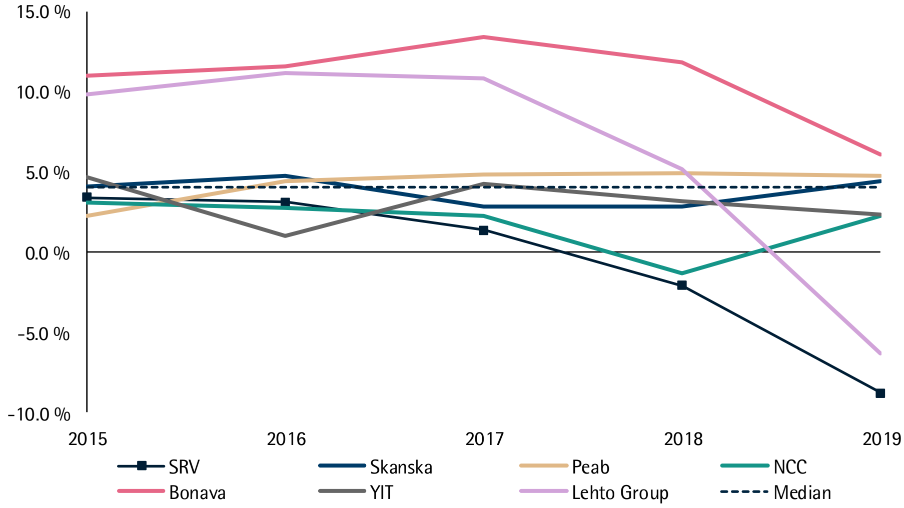


Source: Companies' financial reports, Evli Research

SRV's has seen above peer relative revenue growth (excl. acquisition) in previous years

SRV's revenue growth was the second highest of its competitors in 2016 and 2017, with only Lehto having been able to increase revenues at a faster pace in the past two years, albeit at a clearly lower starting position on absolute revenue figures compared to peers. NCC spun off Bonava in 2016 and historical figures have been adjusted accordingly. YIT had negative revenue 2016 but saw an annual revenue growth of 18.8% in 2017. YIT's figures are adjusted for the acquisition of Lemminkäinen. The year 2018 saw a downward trend in revenue growth for the Finnish peers and SRV posting growth figures below that of the peers. On absolute figures, the included Finnish construction companies grew on aggregate 26.7% in 2017, after which sales growth stalled in 2018, and turned to a growth of 6.2% in 2019. Similar figures for the Swedish construction companies show aggregate sales growth slowing down from 3.3% in 2017 to 0.2% in 2019.

Figure 23: EBIT margin development of SRV's main competitors



Source: Companies' financial reports, Evli Research

Lehto and Bonava have outperformed other Nordic construction companies

SRV and its main competitors have generated a median EBIT margin of 4.1% between 2015 and 2019. Of these companies, Bonava and Lehto Group have outperformed others with EBIT margins significantly above industry median. One of the key reasons for Lehto's success has been its modular business model: it uses repeatable standard solutions in its operations to cut costs. In the construction sector, the productivity has long stagnated and Lehto has been able to increase its productivity with the standard solutions. However, in 2018 and 2019 Lehto's profitability fell significantly due to challenges in the company's renovation business and certain projects. Bonava, which was spun off from NCC in 2016, has also generated impressive EBIT in the recent years. Like Lehto, Bonava has implemented the modular system into its business which in part explains the high EBIT margin it has generated in the past four years. Bonava has also seen margins decline in recent years, in part due to challenges in Finland.

SRV's profitability has not paired with that of peers

Other large Nordic construction companies have had relatively level profit margins in the recent years, although most of the peers followed suite in 2018 and saw y/y declines. SRV has not been able to generate as high profits as its main competitors and the EBIT margin slipped to -2.1% in 2018 and further to -8.8% in 2019. SRV's profitability has in recent years been the weakest compared with the peers. We note however that the underlying construction margins improved in 2019, with the Construction-segment operating profit margin improving to 0.7% (2018: -1.4%). Another note is that SRV's EBIT margin has declined steadily from the 3.6% level in 2014. SRV's profitability has been affected by the hefty use of subcontractors as the subcontractors' pricing power has increased during the recent construction boom. The loss in 2018 is mainly explained by the additional costs related to the REDI shopping centre project while 2019 was affected by significant impairments.

SRV has achieved good revenue growth but the EBIT margin has suffered

Based on competitor comparison, SRV has been rather successful in generating sales growth during the past five years, at the cost of profitability. It has been able to generate a sales CAGR of 9% from 2014 to 2019 while the EBIT margin has fallen to the weakest among peers. SRV's profitability has steadily decreased during the period. EBIT-margins, especially for the Finnish construction companies, have however also fallen in the previous two years.

Estimates

2019 profitability remained weak due to NRI's

SRV's revenue during 2019 amounted to EUR 1,060.9m (10.7% y/y) while the operative operating profit was EUR -96.8m (EUR -10.0m in 2018) and operating profit -93.0m (-19.8m in 2018). Revenue increased slightly in business construction, while housing construction revenue grew clearly due to the completion of a larger number of developer-contracted housing units. Profitability was largely affected by the impairment of the REDI shopping centre and other impairments in the Construction and Investments -segments. Changes in the ruble exchange rate positively affected the operating profit compared to the previous year, caused by the revaluation of euro-denominated loans to rubles and hedging expenses.

Estimates for 2020

Completion of a fewer developer-contracted housing units expected to decrease sales in 2020

We expect group revenue in 2020E to amount to EUR 956.2m (-9.9% y/y). We expect the decline in revenue to derive mainly from the completion of fewer developer-contracted housing units, with company guidance at 586 units (808 units in 2019), while we expect business construction revenue to remain near previous year levels due to continued high activity. We expect profitability to improve substantially with the reduced impact of non-recurring items and expect an operative operating profit of EUR 10.3m (2019: -96.8m).

Business construction revenue supported by long order backlog; housing construction expected to decline from fewer completions

Business construction saw slight sales growth in 2019 of 2.0%, with revenue amounting to EUR 679.7m. The construction activity has remained at a good level following a solid order backlog. The order intake in 2019 was rather weak and as a result the order backlog declined to EUR 861.5m at the end of 2019 (2018: EUR 1,233.3m). We nonetheless expect business construction revenue in 2020 to remain near previous year levels due to order backlog duration and to amount to EUR 668.0m (-1.7% y/y). Housing construction saw a good year in 2019 in terms of revenue with the completion of 808 developer-contracted housing units (2018: 526) and revenue grew 30.7% to EUR 377.9m. The order backlog decreased by 17.2% to 482.7m at the end of 2019. We expect revenue to decline by 24.5% in 2020 with the completion of fewer developer-contracted housing units (2020E: 586, 2019: 808).

Profitability set to improve from healthier construction operations

Profitability in the Construction-segment improved in 2019 as the higher-than-expected costs in the fixed-price REDI project no longer had an impact. Profitability was however burdened by lower than forecasted margins in two projects, completed in 2019, totaling EUR 11.0m, along with expense entries totaling EUR 6.0m relating to the REDI Majakka water damage and some EUR 9.4m in impairments and losses on plots in Russia and Estonia. The operating profit amounted to EUR 7.0m compared with EUR -13.4m in 2018. We expect to see continued improvement in profitability in 2020 with the decrease in impact of NRI's and completion of the two weaker margin projects. The measures taken to improve profitability through SRV's recovery program will also have a positive effect on 2020E. We estimate an operating profit of EUR 21.3m (2020: 7.0m).

Investments-segment profitability seen to remain negative

Revenue in the Investments-segment during 2019 amounted to EUR 5.9m (2018: EUR 4.6m), consisting mainly of revenue from shopping centre management, as SRV owns shopping centers through its associated companies and joint ventures and their revenue is not presented in SRV's consolidated revenue. We expect revenue to decline to EUR 5.7m in 2020 as the sale of the REDI shopping centre will decrease management fees. The operative operating profit amounted to EUR -96.2m in 2019 (EUR -7.8m in 2018), affected by significant impairments relating to the REDI shopping centre, reclassification of Pearl Plaza and other impairments. The operating profit during the same period amounted to EUR -92.4m (EUR -17.6m during 2018). The operating profit was slightly aided by favourable net currency exchange fluctuations (2019: EUR 3.8m) compared with the operative operating profit. We expect profitability to remain negative, with an operating profit in 2020E of EUR -12.0m.

Estimates for 2021-2022

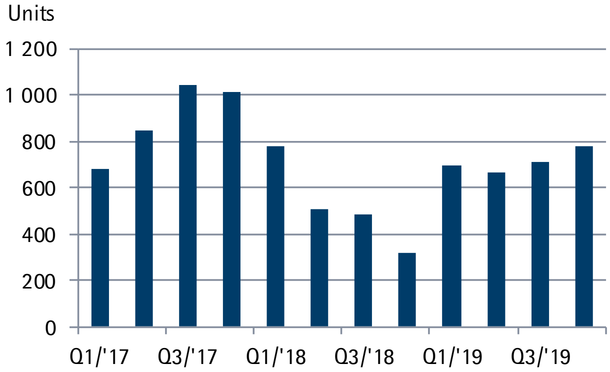
Expect revenue to decline but improvements in profitability

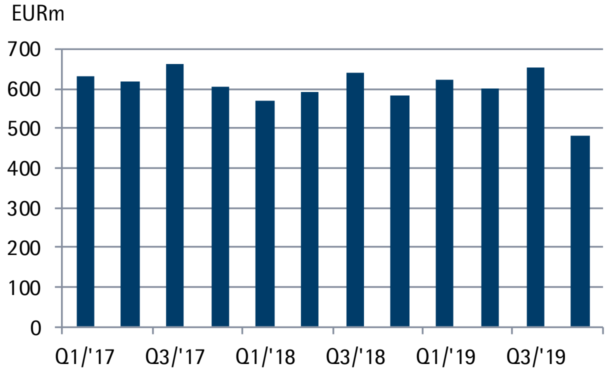
In 2021E and 2022E we expect group revenue of EUR 966.1m and 943.4m respectively. We expect essentially flat revenue growth development in 2021E due to an expected slowdown in Business construction volumes, offset by an expected increase in housing construction revenue y/y. We expect profitability to improve in the coming years and the operative operating profit to amount to EUR 19.9m and 24.0m in 2021E and 2022E respectively. We assume improvements in the profitability of the Construction-segment, mainly due to improved margins from a lesser construction expense burden and the one-offs that have burdened 2019 profitability.

Housing construction revenue expected to decline from solid 2019 levels

We expect housing construction revenue to improve slightly in 2021E from the levels expected in 2020E following the expected completion of fewer developer contracting housing units. Housing construction typically follows a two-year cycle and the pick-up in developer-contracted housing unit start-ups in 2019 should be visible in 2021E. In 2021E and 2022E we expect revenue of EUR 328.7m and 315.5m respectively. The order book and total units under construction declined around 20% from previous year levels following the completion of a substantial amount of housing units in Q4/19. A significant contract for the construction of housing units worth some EUR 197m, signed in Q1/2020, alleviates some of the larger concerns regarding order backlog improvement.

Figure 24: Housing construction in Finland developer contracting start-ups (R12m) and order backlog (end of quarter)



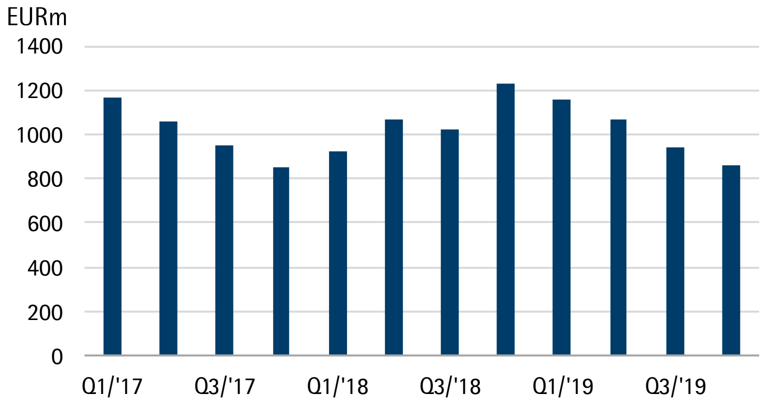


Source: SRV, Evli research

Business construction volumes expected to decline

In business construction we expect revenue of EUR 634.6m and 625.1m in 2021E and 2022E respectively. We expect to see a decline in revenue following an expected lower construction activity and weaker order backlog. Volumes in non-housing construction in Finland and commercial- and office-buildings in particular, are in general seen to decline in the coming years after previous boom years. SRV has several large projects on-going, for instance the Tampere Deck and Arena and the Helsinki Airport T2 expansion project, which we expect to support in keeping volumes at healthy levels.

Figure 25: Business construction order backlog (end of quarter)



Source: SRV, Evli research

Investments-segment profitability expected to improve, uncertainty factors significant

In the Investments-segment earnings uncertainty is high, as profitability is dependent on the highly non-transparent share of profits of the associated and JV companies and the Euro to Ruble exchange rate. Shopping centre divestments may also have a significant impact on earnings. We expect the profitability of the Investments-segment to remain negative but improve during 2021-2022E, as the shopping centres achieve higher occupancy rates and rent levels improve. Revenue mainly arises from fees for managing the shopping centres and with no new shopping centres to be completed we do not expect any larger growth in revenue. The result of the Investments-segment is also dependent upon possible exits from the constructed shopping centres, which will increase in likelihood during the coming years.

Pearl Plaza exit would ease balance sheet burdens

We have not included estimates for the potential exits of shopping centers in our income statement estimates due to the timing and completion uncertainty but have included cash flow estimates and valued cash flows from the projects separately. SRV announced in February 2018 that it is investigating the possible sale of the Pearl Plaza shopping center and has since signed a cooperation agreement regarding the sale of the property. At the end of 2019 SRV further classified Pearl plaza as an asset held for sale. We have estimated an exit in 2020 but emphasize that the real estate situation in St. Petersburg has been troublesome, although vacancy rates have been shrinking and the economy has seen some recovery. The timing and terms of an exit therefore involve high uncertainty. SRV has earlier noted that a possible transaction would have no significant profit impact. The release of capital tied up in the shopping centre would however have a positive impact and ease some of SRV's balance sheet burden.

Table 3: Estimates summary

SRV	2018	Q1/'19	Q2/'19	Q3/'19	Q4/'19	2019	Q1/'20E	Q2/'20E	Q3/'20E	Q4/'20E	2020E	2021E	2022E
Revenue	**959.6**	**222.6**	**207.4**	**227.1**	**403.9**	**1 060.9**	**187.0**	**243.4**	**205.8**	**319.9**	**956.2**	**966.1**	**943.4**
change, %	*-13.9%*	*3.2%*	*-12.0%*	*8.9%*	*34.7%*	*10.6%*	*-16.0%*	*17.4%*	*-9.4%*	*-20.8%*	*-9.9%*	*1.0%*	*-2.3%*
Operative operating profit	**-10.1**	**0.5**	**-3.1**	**-7.0**	**-87.2**	**-96.9**	**0.9**	**3.8**	**1.5**	**4.1**	**10.3**	**19.9**	**24.0**
-margin	*-1.1%*	*0.2%*	*-1.5%*	*-3.1%*	*-21.6%*	*-9.1%*	*0.5%*	*1.6%*	*0.7%*	*1.3%*	*1.1%*	*2.1%*	*2.5%*
Items affecting comparability*	-9.8	2.8	0.0	0.6	0.4	3.8	-6.0	0.0	0.0	0.0	-6.0	0.0	0.0
Operating profit	**-19.9**	**3.3**	**-3.2**	**-6.3**	**-86.8**	**-93.0**	**-5.1**	**3.8**	**1.5**	**4.1**	**4.3**	**19.9**	**24.0**
-margin	*-2.1%*	*1.5%*	*-1.5%*	*-2.8%*	*-21.5%*	*-8.8%*	*-2.7%*	*1.6%*	*0.7%*	*1.3%*	*0.4%*	*2.1%*	*2.5%*
Net financials	-17.5	-3.6	-7.7	-7.6	-10.4	-29.3	-6.0	-6.0	-6.0	-6.0	-24.0	-20.0	-20.0
Pre-tax profit	**-37.3**	**-0.3**	**-10.8**	**-14.0**	**-97.2**	**-122.4**	**-11.1**	**-2.2**	**-4.5**	**-1.9**	**-19.7**	**-0.1**	**4.0**
Income taxes	6.1	0.7	1.9	2.3	13.8	18.7	2.2	0.4	0.9	0.4	3.9	0.0	-0.8
Non-controlling interest	1.1	-0.7	0.0	-0.1	0.1	-0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net earnings	**-30.1**	**-0.4**	**-9.0**	**-11.7**	**-83.3**	**-104.4**	**-8.9**	**-1.8**	**-3.6**	**-1.5**	**-15.8**	**-0.1**	**3.2**
EPS rep.**	**-0.56**	**-0.02**	**-0.18**	**-0.22**	**-1.43**	**-1.85**	**-0.06**	**-0.01**	**-0.03**	**-0.01**	**-0.11**	**0.00**	**0.02**

Construction	2018	Q1/'19	Q2/'19	Q3/'19	Q4/'19	2019	Q1/'20E	Q2/'20E	Q3/'20E	Q4/'20E	2020E	2021E	2022E
Revenue	**955.4**	**221.9**	**206.7**	**225.9**	**403.1**	**1 057.6**	**186.3**	**242.7**	**205.1**	**319.2**	**953.4**	**963.3**	**940.6**
change, %		*3.4%*	*-11.9%*	*8.8%*	*35.0%*	*10.7%*	*-16.0%*	*17.4%*	*-9.2%*	*-20.8%*	*-9.9%*	*1.0%*	*-2.4%*
Business construction	**666.3**	**145.4**	**162.6**	**171.2**	**200.5**	**679.7**	**151.0**	**162.2**	**171.0**	**183.8**	**668.0**	**634.6**	**625.1**
change, %	*-7.0%*	*-6.4%*	*-2.5%*	*6.8%*	*9.0%*	*2.0%*	*3.9%*	*-0.3%*	*-0.1%*	*-8.3%*	*-1.7%*	*-5.0%*	*-1.5%*
Housing construction	**289.1**	**77.0**	**43.6**	**54.7**	**202.6**	**377.9**	**35.3**	**80.5**	**34.1**	**135.4**	**285.4**	**328.7**	**315.6**
change, %	*-23.9%*	*29.8%*	*-35.7%*	*15.4%*	*76.8%*	*30.7%*	*-54.2%*	*84.7%*	*-37.6%*	*-33.2%*	*-24.5%*	*15.2%*	*-4.0%*
Operating profit	**-13.4**	**4.8**	**2.0**	**-3.5**	**3.6**	**7.0**	**3.4**	**6.3**	**4.0**	**7.6**	**21.3**	**28.9**	**31.0**
-margin	*-1.4%*	*2.2%*	*1.0%*	*-1.5%*	*0.9%*	*0.7%*	*1.8%*	*2.6%*	*2.0%*	*2.4%*	*2.2%*	*3.0%*	*3.3%*

Investments	2018	Q1/'19	Q2/'19	Q3/'19	Q4/'19	2019	Q1/'20E	Q2/'20E	Q3/'20E	Q4/'20E	2020E	2021E	2022E
Revenue	**4.6**	**1.3**	**1.5**	**1.4**	**1.7**	**5.9**	**1.2**	**1.2**	**1.2**	**1.2**	**4.8**	**4.8**	**4.8**
change, %		*8.3%*	*25.0%*	*16.7%*	*70.0%*	*28.3%*	*-7.7%*	*-20.0%*	*-14.3%*	*-29.4%*	*-18.6%*	*0.0%*	*0.0%*
Operative operating profit	**-7.8**	**-2.7**	**-1.9**	**-3.7**	**-87.9**	**-96.2**	**-1.5**	**-1.5**	**-1.5**	**-1.5**	**-6.0**	**-4.0**	**-2.0**
Items affecting comparability*	-9.8	2.8	0.0	0.6	0.4	3.8	-6.0	0.0	0.0	0.0	-6.0	0.0	0.0
Operating profit	**-17.6**	**0.1**	**-1.9**	**-3.1**	**-87.5**	**-92.4**	**-7.5**	**-1.5**	**-1.5**	**-1.5**	**-12.0**	**-4.0**	**-2.0**

Other operations and elim.	2018	Q1/'19	Q2/'19	Q3/'19	Q4/'19	2019	Q1/'20E	Q2/'20E	Q3/'20E	Q4/'20E	2020E	2021E	2022E
Revenue	-0.4	-0.6	-0.8	-0.3	-0.9	-2.6	-0.5	-0.5	-0.5	-0.5	-2.0	-2.0	-2.0
Operating profit	11.1	-1.6	-3.2	0.2	-2.9	-7.6	-1.0	-1.0	-1.0	-2.0	-5.0	-5.0	-5.0

*Foreign exchange rate impact, **incl. tax adjusted hybrid interest

Source: Evli research, SRV

Valuation

HOLD-rating with a target price of EUR 1.00 (1.30)

We base our valuation mainly on our DCF-model and SOTP-approach, as on our estimates near-term profitability figures are expected to remain weak and high financial expenses keep earnings in the red. The value of balance sheet objects are in our view also better captured through the aforementioned approaches, when comparing with a peer-multiple approach. Our DCF and SOTP implied equity fair values are EUR 1.10 and 0.64 respectively. We derive a target price or EUR 1.00 (1.30) per share, assigning more weight to our DCF fair value due to an unjust near-term weight on profitability of our SOTP-model and retain our HOLD-rating.

Table 4: Valuation summary

VALUATION						
	METRIC	Est., EURm	Multiple	EV	Per share*	Comments
Construction	EV/EBIT 20E	21	9.0x	192	1.26	Construction peers
4Daily	NPV	6	1x	6	0.04	Exit '22, yld. 10 %
Okhta mall	NPV	55	1x	55	0.36	Exit '22, yld. 10 %
Investments plots	BV	64	0.7x	45	0.30	2019
Assets held for sale	BV	69	1x	69	0.46	2019
Other operations		-5	10x	-50	-0.33	
Net debt				-220	-1.45	2020E
Equity value	SOTP			97	0.64	
Equity value	DCF				1.10	
Target price (EUR)					**0.95**	

Source: Evli Research

Source: Evli Research, *assuming ~152m shares, described more in detail below

Our SOTP approach takes into account our 2020E EBIT estimate for construction operations, at a 9.0x multiple, based on peer median multiples, along with separate NPV's for Okhta mall and 4Daily. We note a clear recent decline in construction sector multiples, with the peer median EV/EBIT having declined some 30% from the pre-Corona peak. The assets held for sale (REDI, Tampere Deck and Arena, and Pearl Plaza are included at 2019 book value. Land-areas and plot-owning companies owned in the Investments segment are included at 0.7x FY2019 book value. Other operations include mainly other operations and eliminations. Deducting expect net debt at the end of 2020 after the planned financial measures gives an equity value of EUR 0.64 per share.

In deriving the per share SOTP-value we have made preliminary assumptions regarding the announced actions to improve financial stability. Due to lack of further information, we have assumed that both share issues will be completed to the amount of given commitments announced in February 2020 and a subscription price of EUR 1.05 in both share issues, which corresponds to the subscription price that commitments for the first planned issue were given at. This would result in an estimated total of EUR 95.5m (57m hybrid conversion + 40m share issue – expense est. EUR 1.5m) decrease in net debt and an increase in shares of 92.4m to a total of 151.96m.

Table 5: Shopping center NPV assumptions

	Okhta Mall	4Daily
Ownership	45% + 15%	18.7%
Debt financing, EURm	100	30
Exit year	2022	2022
Target net rental income, EURm	24	7.5
Exit yield	10%	10%
Exit price, EURm	240	75
WACC	13%	13%
SRV's share of cash flows, EURm	54.9	5.9

Source: Evli research

On our estimates SRV trades clearly above the peer median multiples. SRV's multiples are affected by the leveraged balance sheet, with financial expenses burdening earnings, while we also estimate profitability to remain below target levels in the coming years. We do not assign any significant weight on multiples due to the value of items on the balance sheet not reflected in earnings figures.

Table 6: SRV peer group multiples

	MCAP	EV/EBITDA			EV/EBIT			P/E		
SRV PEER GROUP	MEUR	20	21	22	20	21	22	20	21	22
Skanska	5584	6.7x	6.2x	5.6x	8.4x	7.8x	7.1x	10.0x	9.2x	8.4x
Peab	1827	7.3x	7.0x	6.6x	9.0x	9.7x	9.3x	9.1x	8.6x	8.1x
NCC	1245	6.0x	5.6x	5.4x	9.7x	8.6x	8.1x	9.4x	8.3x	7.7x
AF Gruppen	1171	6.5x	6.2x	6.0x	8.2x	7.7x	7.8x	13.3x	12.7x	11.6x
Veidekke	953	7.2x	6.7x	6.2x	12.0x	11.0x	9.6x	9.2x	8.4x	7.8x
JM	1081	8.1x	7.7x	7.1x	8.0x	7.6x	7.0x	7.9x	7.5x	6.9x
Bonava	429	7.9x	8.3x	7.0x	8.3x	8.7x	7.2x	4.9x	5.1x	4.1x
YIT	803	7.7x	7.7x	7.2x	10.6x	9.8x	9.5x	7.7x	7.0x	6.5x
Lehto Group	79	9.5x	6.9x	5.5x	13.0x	8.5x	6.8x	7.7x	4.5x	3.5x
Peer Group Average	1463	**7.4x**	**6.9x**	**6.3x**	**9.7x**	**8.8x**	**8.0x**	**8.8x**	**7.9x**	**7.2x**
Peer Group Median	1081	**7.3x**	**6.9x**	**6.2x**	**9.0x**	**8.6x**	**7.8x**	**9.1x**	**8.3x**	**7.7x**
SRV (Evli est.)*	**55**	**23.0x**	**16.4x**	**14.0x**	**42.2x**	**23.1x**	**18.7x**	**neg.**	**neg.**	**neg.**
SRV prem./disc. to peer median		*>100%*	*>100%*	*>100%*	*>100%*	*>100%*	*>100%*	-	-	-

*Source FactSet, Evli Research. *EBIT: Operative operating profit*

Risks

Coronavirus imposes increased near-term uncertainty

We note that the on-going outbreak of the coronavirus has created significant short-term uncertainty. In our view the construction sector in Finland is more resilient to the possible impact of the virus than average, as the order backlog is typically long and the continued need for new housing in growth centres will continue. So far, the outbreak has not materially affected SRV's operations. The construction sector, however, has seen several signs of co-operation negotiations and temporary layoffs, as constructors are delaying new projects. In our view the possible key near-term risks are the following:

1) Supply chain issues: the construction industry is dependent upon a broad supply chain and the availability of material may delay construction projects
2) Temporary construction halts: quarantines due to virus cases or suspicions of such may temporarily close down parts of or entire construction sites
3) Work force availability: travel restrictions and quarantines imposed for workforce of foreign nationality may affect availability of workforce. Close to one third of SRV's workforce consists of foreign labour. SRV has been able to manage the situation well while some constructors have had issues with retaining the workforce
4) Fall in housing demand: a decline in Finns view on the economy and employment situation may deter the purchase of housing units and affect the sales of new units as well as housing prices. We expect a majority of SRV's developer-contracted housing units in 2020 to be completed in Q4 and thus any clear signs of changes in purchase behaviour should be seen in the latter half of the year
5) Increased exit challenges: real estate transaction volumes may be affected by any increased economic turmoil and postpone any anticipated divestments

We further note that the collapse of the OPEC+ production agreement significantly weakened the Ruble in relation to the Euro. SRV has exposure to the exchange rates through its joint ventures in Russia. We expect the weakening of the Ruble to have a clear negative impact on Q1/2020 operating profit but note that the effect is a non-cash item. Any added market turmoil should also not favour SRV in its ambitions to divest its ownership of the properties in Russia.

VALUATION RESULTS		BASE CASE DETAILS		VALUATION ASSUMPTIONS		ASSUMPTIONS FOR WACC	
Current share price	0.92	PV of Free Cash Flow	342	Long-term growth, %	2.0	Risk-free interest rate, %	2.25
DCF share value	1.10	PV of Horizon value	329	WACC, %	7.4	Market risk premium, %	5.8
Share price potential, %	19.3	Unconsolidated equity	1	Spread, %	0.5	Debt risk premium, %	3.5
Maximum value	1.5	Marketable securities	28	Minimum WACC, %	6.9	Equity beta coefficient	1.40
Minimum value	0.8	Debt - dividend	-533	Maximum WACC, %	7.9	Target debt ratio, %	60
Horizon value, %	49.1	Value of stock	167	Nr of shares, Mn	152.0	Effective tax rate, %	20

DCF valuation, EURm	2019	2020E	2021E	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	Horizon
Net sales	1,061	956	966	943	962	982	1,001	1,021	1,042	1,062	1,084	1,106
Sales growth, %	*10.5*	*-9.9*	*1.0*	*-2.3*	*2.0*	*2.0*	*2.0*	*2.0*	*2.0*	*2.0*	*2.0*	*2.0*
Operating income (EBIT)	-93	4	20	24	34	39	40	41	42	42	43	44
Operating income margin, %	*-8.8*	*0.4*	*2.1*	*2.5*	*3.5*	*4.0*	*4.0*	*4.0*	*4.0*	*4.0*	*4.0*	*4.0*
+ Depreciation+amort.	90	9	8	8	8	8	8	8	8	8	8	
EBITDA	-3	13	28	32	42	47	48	49	50	50	51	
- Paid taxes	-6	-1	-4	-5	-7	-8	-8	-8	-8	-8	-9	
- Change in NWC	-75	51	-25	6	5	5	-5	-5	-5	-5	-5	
NWC / Sales, %	*31.3*	*29.3*	*31.6*	*31.7*	*30.6*	*29.5*	*29.4*	*29.4*	*29.3*	*29.2*	*29.1*	
+ Change in other liabs	-4	0	0	0	0	0	0	0	0	0	0	
- Operative CAPEX	-201	-2	-2	-2	-2	-2	-2	-2	-3	-3	-3	
opCAPEX / Sales, %	*2.5*	*0.6*	*0.6*	*0.5*	*0.7*	*0.7*	*0.7*	*0.6*	*0.6*	*0.6*	*0.6*	
- Acquisitions	0	0	0	0	0	0	0	0	0	0	0	
+ Divestments	0	0	0	0	0	0	0	0	0	0	0	
- Other items	172	40	-3	58	0	0	35	0	0	0	0	
= FCFF	-38	101	-6	89	37	42	68	33	34	34	34	659
= Discounted FCFF		96	-6	73	28	30	45	20	19	18	17	329

= DFCF min WACC		96	-6	74	29	30	46	21	20	19	18	380
= DFCF max WACC		96	-6	72	28	29	44	20	19	18	16	288

INTERIM FIGURES

EVLI ESTIMATES, EURm	2019Q1	2019Q2	2019Q3	2019Q4	2019	2020Q1E	2020Q2E	2020Q3E	2020Q4E	2020E	2021E	2022E
Net sales	222.6	207.4	227.1	403.9	1,061.0	187.0	243.4	205.8	319.9	956.2	966.1	943.4
EBITDA	6.2	-0.9	-2.0	-6.4	-3.1	-3.1	5.8	3.5	6.6	12.8	28.1	32.2
EBITDA margin (%)	*2.8*	*-0.4*	*-0.9*	*-1.6*	*-0.3*	*-1.7*	*2.4*	*1.7*	*2.1*	*1.3*	*2.9*	*3.4*
EBIT	3.3	-3.1	-6.4	-86.9	-93.1	-5.1	3.8	1.5	4.1	4.3	19.9	24.0
EBIT margin (%)	*1.5*	*-1.5*	*-2.8*	*-21.5*	*-8.8*	*-2.7*	*1.6*	*0.7*	*1.3*	*0.4*	*2.1*	*2.5*
Net financial items	-3.6	-7.7	-7.6	-10.4	-29.3	-6.0	-6.0	-6.0	-6.0	-24.0	-20.0	-20.0
Pre-tax profit	-0.3	-10.8	-14.0	-97.3	-122.4	-11.1	-2.2	-4.5	-1.9	-19.7	-0.1	4.0
Tax	0.7	1.9	2.3	13.8	18.7	2.2	0.4	0.9	0.4	3.9	0.0	-0.8
Tax rate (%)	*233.3*	*17.6*	*16.4*	*14.2*	*15.3*	*20.0*	*20.0*	*20.0*	*20.0*	*20.0*	*20.0*	*20.0*
Net profit	0.1	-9.8	-12.6	-84.7	-107.2	-11.2	-2.8	-4.4	-2.4	-20.8	-3.4	-0.1
EPS	0.00	-0.17	-0.21	-1.42	-1.80	-0.07	-0.02	-0.03	-0.02	-0.14	-0.02	0.00
EPS adjusted (diluted no. of shares)	0.00	-0.17	-0.21	-1.42	-1.80	-0.07	-0.02	-0.03	-0.02	-0.14	-0.02	0.00
Dividend per share	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.03
SALES, EURm												
Construction	221.9	206.7	226.0	403.1	1,057.7	186.3	242.7	205.1	319.2	953.4	963.3	940.6
Investments	1.3	1.5	1.4	1.7	5.9	1.2	1.2	1.2	1.2	4.8	4.8	4.8
Other	-0.6	-0.8	-0.3	-0.9	-2.6	-0.5	-0.5	-0.5	-0.5	-2.0	-2.0	-2.0
Total	222.6	207.4	227.1	403.9	1,061.0	187.0	243.4	205.8	319.9	956.2	966.1	943.4
SALES GROWTH, Y/Y %												
Construction	*3.3*	*-11.9*	*8.9*	*35.1*	*10.7*	*-16.0*	*17.4*	*-9.2*	*-20.8*	*-9.9*	*1.0*	*-2.4*
Investments	*8.3*	*25.0*	*16.7*	*70.0*	*28.3*	*-7.7*	*-20.0*	*-14.3*	*-29.4*	*-18.6*	*0.0*	*0.0*
Other	*100.0*	*0.0*	*200.0*	*-400.0*	*2,500.0*	*-16.7*	*-37.5*	*66.7*	*-44.4*	*-23.1*	*0.0*	*0.0*
Total	*3.2*	*-12.0*	*8.8*	*34.8*	*10.5*	*-16.0*	*17.4*	*-9.4*	*-20.8*	*-9.9*	*1.0*	*-2.3*
EBIT, EURm												
Construction	4.8	2.0	-3.5	3.7	7.0	3.4	6.3	4.0	7.6	21.3	28.9	31.0
Investments	0.1	-1.9	-3.1	-87.6	-92.5	-7.5	-1.5	-1.5	-1.5	-12.0	-4.0	-2.0
Other	-1.6	-3.2	0.2	-3.0	-7.6	-1.0	-1.0	-1.0	-2.0	-5.0	-5.0	-5.0
Total	3.3	-3.1	-6.4	-86.9	-93.1	-5.1	3.8	1.5	4.1	4.3	19.9	24.0
EBIT margin, %												
Construction	*2.2*	*1.0*	*-1.5*	*0.9*	*0.7*	*1.8*	*2.6*	*2.0*	*2.4*	*2.2*	*3.0*	*3.3*
Investments	*7.7*	*-126.7*	*-221.4*	*-5,152.9*	*-1,567.8*	*-625.0*	*-125.0*	*-125.0*	*-125.0*	*-250.0*	*-83.3*	*-41.7*
Other	*266.7*	*400.0*	*-66.7*	*333.3*	*292.3*	*200.0*	*200.0*	*200.0*	*400.0*	*250.0*	*250.0*	*250.0*
Total	*1.5*	*-1.5*	*-2.8*	*-21.5*	*-8.8*	*-2.7*	*1.6*	*0.7*	*1.3*	*0.4*	*2.1*	*2.5*

INCOME STATEMENT, EURm	2015	2016	2017	2018	2019	2020E	2021E	2022E
Sales	719.2	884.0	1,114.1	959.9	1,061.0	956.2	966.1	943.4
Sales growth (%)	*5.1*	*22.9*	*26.0*	*-13.8*	*10.5*	*-9.9*	*1.0*	*-2.3*
EBITDA	28.0	34.2	21.1	-14.6	-3.1	12.8	28.1	32.2
EBITDA margin (%)	*3.9*	*3.9*	*1.9*	*-1.5*	*-0.3*	*1.3*	*2.9*	*3.4*
Depreciation	-3.5	-6.6	-5.7	-5.3	-90.0	-8.5	-8.2	-8.1
EBITA	24.5	27.6	15.4	-19.9	-93.1	4.3	19.9	24.0
Goodwill amortization / writedown	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EBIT	24.5	27.6	15.4	-19.9	-93.1	4.3	19.9	24.0
EBIT margin (%)	*3.4*	*3.1*	*1.4*	*-2.1*	*-8.8*	*0.4*	*2.1*	*2.5*
Reported EBIT	24.5	27.6	15.4	-19.9	-14.7	4.3	19.9	24.0
EBIT margin (reported) (%)	*3.4*	*3.1*	*1.4*	*-2.1*	*-1.4*	*0.4*	*2.1*	*2.5*
Net financials	-6.9	-11.3	-10.7	-17.5	-29.3	-24.0	-20.0	-20.0
Pre-tax profit	17.6	16.3	4.7	-37.4	-122.4	-19.7	-0.1	4.0
Taxes	-3.6	-2.1	1.2	6.1	18.7	3.9	0.0	-0.8
Minority shares	0.0	0.0	0.2	1.1	0.7	0.0	0.0	0.0
Net profit	9.6	9.2	2.2	-34.1	-28.8	-20.8	-3.4	-0.1
Cash NRIs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Non-cash NRIs	0.0	0.0	0.0	0.0	78.4	0.0	0.0	0.0
BALANCE SHEET, EURm								
Assets								
Fixed assets	263	295	287	273	122	122	122	122
Goodwill	2	2	2	2	2	2	2	2
Right of use assets	0	0	0	173	149	147	145	142
Inventory	337	400	419	438	372	335	339	331
Receivables	119	122	146	122	204	165	189	186
Liquid funds	35	55	24	93	28	110	77	75
Total assets	763	883	889	1,120	913	917	910	893
Liabilities								
Shareholder's equity	231	252	240	191	95	166	163	163
Minority interest	1	-2	-2	-3	-2	-2	-2	-2
Convertibles	45	45	45	45	83	32	32	32
Lease liabilities	0	0	0	174	150	147	145	142
Deferred taxes	2	4	5	5	3	3	3	3
Interest bearing debt	266	301	321	375	300	310	306	298
Non-interest bearing current liabilities	202	253	252	304	244	220	222	217
Other interest-free debt	4	14	18	9	21	21	21	21
Total liabilities	763	883	889	1,120	914	917	910	893
CASH FLOW, EURm								
+ EBITDA	28	34	21	-15	-3	13	28	32
- Net financial items	-7	-11	-11	-17	-29	-24	-20	-20
- Taxes	-3	-2	0	-1	-1	4	0	-1
- Increase in Net Working Capital	29	-15	-44	56	-75	51	-25	6
+/- Other	-3	15	2	2	98	40	-3	58
= Cash flow from operations	44	21	-33	26	-11	84	-20	75
- Capex	-118	-13	-24	-15	-26	-6	-6	-5
- Acquisitions	0	0	0	0	0	0	0	0
+ Divestments	0	0	0	0	0	0	0	0
= Free cash flow	-74	8	-57	11	-37	78	-26	71
+/- New issues/buybacks	47	15	-8	-12	-67	92	0	0
- Paid dividend	-5	-6	-6	-4	0	0	0	0
+/- Other	49	2	40	75	39	-88	-6	-73
Change in cash	17	20	-31	70	-65	82	-33	-2

KEY FIGURES	2016	2017	2018	2019	2020E	2021E	2022E
M-cap	322	214	101	81	55	55	55
Net debt (excl. convertibles)	246	298	456	422	347	374	364
Enterprise value	611	555	601	584	433	460	450
Sales	884	1,114	960	1,061	956	966	943
EBITDA	34	21	-15	-3	13	28	32
EBIT	28	15	-20	-93	4	20	24
Pre-tax	16	5	-37	-122	-20	0	4
Earnings	9	2	-34	-107	-21	-3	0
Equity book value (excl. minorities)	252	240	191	95	166	163	163
Valuation multiples							
EV/sales	0.7	0.5	0.6	0.6	0.5	0.5	0.5
EV/EBITDA	17.9	26.3	-41.1	-188.5	33.9	16.4	14.0
EV/EBITA	22.2	36.1	-30.2	-6.3	101.3	23.1	18.7
EV/EBIT	22.2	36.1	-30.2	-6.3	101.3	23.1	18.7
EV/OCF	28.8	-17.1	23.5	-54.5	5.2	-22.9	6.0
EV/FCFF	-20.4	-10.6	26.3	-15.2	4.3	-71.8	5.0
P/FCFE	40.1	-3.8	9.5	-2.2	1.8	-5.3	2.0
P/E	35.1	98.6	-3.0	-0.8	-6.7	-40.6	-1,076.0
P/B	1.3	0.9	0.5	0.9	0.3	0.3	0.3
Target EV/EBITDA	*0.0*	*0.0*	*0.0*	*0.0*	*41.4*	*19.8*	*17.0*
Target EV/EBIT	*0.0*	*0.0*	*0.0*	*0.0*	*123.6*	*27.9*	*22.7*
Target EV/FCF	*0.0*	*0.0*	*0.0*	*0.0*	*6.8*	*-21.1*	*7.7*
Target P/B	*0.0*	*0.0*	*0.0*	*0.0*	*0.9*	*0.9*	*0.9*
Target P/E	*0.0*	*0.0*	*0.0*	*0.0*	*-7.3*	*-44.1*	*-1,169.6*
Per share measures							
Number of shares	59,500	59,500	59,581	59,581	151,962	151,962	151,962
Number of shares (diluted)	59,500	59,500	59,581	59,581	151,962	151,962	151,962
EPS	0.15	0.04	-0.57	-1.80	-0.14	-0.02	0.00
Operating cash flow per share	0.36	-0.55	0.43	-0.18	0.55	-0.13	0.50
Free cash flow per share	0.14	-0.96	0.18	-0.62	0.51	-0.17	0.47
Book value per share	4.25	4.03	3.21	1.59	1.09	1.07	1.07
Dividend per share	0.10	0.06	0.00	0.00	0.00	0.00	0.03
Dividend payout ratio, %	64.5	164.3	0.0	0.0	0.0	0.0	-3,508.8
Dividend yield, %	1.8	1.7	0.0	0.0	0.0	0.0	3.3
FCF yield, %	2.5	-26.6	10.6	-45.6	142.7	-48.1	129.2
Efficiency measures							
ROE	3.8	0.9	-15.8	-74.9	-15.9	-2.1	-0.1
ROCE	5.2	3.5	-2.1	-12.1	1.9	4.3	5.0
Financial ratios							
Inventories as % of sales	45.3	37.6	45.7	35.1	35.1	35.1	35.1
Receivables as % of sales	13.7	13.1	12.7	19.2	17.3	19.6	19.7
Non-interest bearing liabilities as % of sales	28.7	22.7	31.7	23.0	23.0	23.0	23.0
NWC/sales, %	30.4	28.0	26.7	31.3	29.3	31.6	31.7
Operative CAPEX/sales, %	1.5	2.2	1.5	2.5	0.6	0.6	0.5
CAPEX/sales (incl. acquisitions), %	1.5	2.2	1.5	2.5	0.6	0.6	0.5
FCFF/EBITDA	-0.9	-2.5	-1.6	12.4	7.9	-0.2	2.8
Net debt/EBITDA, book-weighted	7.2	14.1	-31.2	-136.2	27.2	13.3	11.3
Debt/equity, market-weighted	0.9	1.5	3.7	3.7	5.7	5.6	5.4
Equity ratio, book-weighted	36.1	35.5	23.6	21.2	23.6	23.4	23.9
Gearing, %	83.4	105.0	195.1	240.4	177.0	193.8	189.0

COMPANY DESCRIPTION: SRV is a Finnish project management contractor that develops and builds commercial and business premises, residential units as well as infrastructure and logistics projects. The company is also an investor in and manager of several shopping centres. The company operates in Finland and Russia.

INVESTMENT CASE: SRV's road has been bumpy in the past few years and earnings have been in the red despite a construction boom and record high revenue levels. The expected slow-down in construction volumes should alleviate supply chain pressures and along with profitability improvement measures to be taken support bottom-line figures. Successful exits from developed shopping centres remain crucial in improving the company's balance sheet.

OWNERSHIP STRUCTURE	SHARES	EURm	%
Kolpi Investments Oy	11,505,457	4.150	7.6%
Kokkila Timo Tapani	7,617,216	2.748	5.0%
Kokkila Tuomas	6,494,422	2.343	4.3%
Kokkila Lauri	6,494,422	2.343	4.3%
Tiiviste-Group Oy	6,111,821	2.205	4.0%
Nordea Life Insurance Finland Ltd.	1,720,685	0.621	1.1%
The State Pension Fund	1,170,000	0.422	0.8%
Ilmarinen Mutual Pension Insurance Company	962,822	0.347	0.6%
SRV Yhtiöt Oyj	918,599	0.331	0.6%
OP-Suomi Value fund	716,666	0.259	0.5%
Ten largest	43,712,110	15.767	29%
Residual	108,249,790	39.047	71%
Total	151,961,900	54.814	100%

EARNINGS CALENDAR	
April 29, 2020	Q1 report
July 21, 2020	Q2 report
October 29, 2020	Q3 report
OTHER EVENTS	
March 26, 2020	AGM

COMPANY MISCELLANEOUS	
CEO: Saku Sipola	Tarvonsalmenkatu 15, Espoo
CFO: Ilkka Pitkänen	Tel: +358 20 145 5200
IR:	

DEFINITIONS

P/E $\frac{\text{Price per share}}{\text{Earnings per share}}$	**EPS** $\frac{\text{Profit before extraord. items and taxes– income taxes + minority interest}}{\text{Number of shares}}$
P/BV $\frac{\text{Price per share}}{\text{Shareholders' equity + taxed provisions per share}}$	**DPS** Dividend for the financial period per share
Market cap Price per share * Number of shares	**OCF (Operating cash flow)** EBITDA – Net financial items – Taxes – Increase in working capital – Cash NRIs ± Other adjustments
EV (Enterprise value) Market cap + net debt + minority interest at market value – share of associated companies at market value	**FCF (Free cash flow)** Operating cash flow – operative CAPEX – acquisitions + divestments
EV/Sales $\frac{\text{Enterprise value}}{\text{Sales}}$	**FCF yield, %** $\frac{\text{Free cash flow}}{\text{Market cap}}$
EV/EBITDA $\frac{\text{Enterprise value}}{\text{Earnings before interest, tax, depreciation and amortization}}$	**Operative CAPEX/sales** $\frac{\text{Capital expenditure – divestments – acquisitions}}{\text{Sales}}$
EV/EBIT $\frac{\text{Enterprise value}}{\text{Operating profit}}$	**Net working capital** Current assets – current liabilities
Net debt Interest bearing debt – financial assets	**Capital employed/Share** $\frac{\text{Total assets – non-interest bearing debt}}{\text{Number of shares}}$
Total assets Balance sheet total	**Gearing** $\frac{\text{Net debt}}{\text{Equity}}$
Div yield, % $\frac{\text{Dividend per share}}{\text{Price per share}}$	**Debt/Equity, %** $\frac{\text{Interest bearing debt}}{\text{Shareholders' equity + minority interest + taxed provisions}}$
Payout ratio, % $\frac{\text{Total dividends}}{\text{Earnings before extraordinary items and taxes – income taxes + minority interest}}$	**Equity ratio, %** $\frac{\text{Shareholders' equity + minority interest + taxed provisions}}{\text{Total assets – interest-free loans}}$
ROCE, % $\frac{\text{Profit before extraordinary items + interest expenses+ other financial costs}}{\text{Balance sheet total – non-interest bearing debt (average)}}$	**CAGR, %** Cumulative annual growth rate = Average growth per year
ROE, % $\frac{\text{Profit before extraordinary items and taxes – income taxes}}{\text{Shareholder's equity + minority interest + taxed provisions (average)}}$	

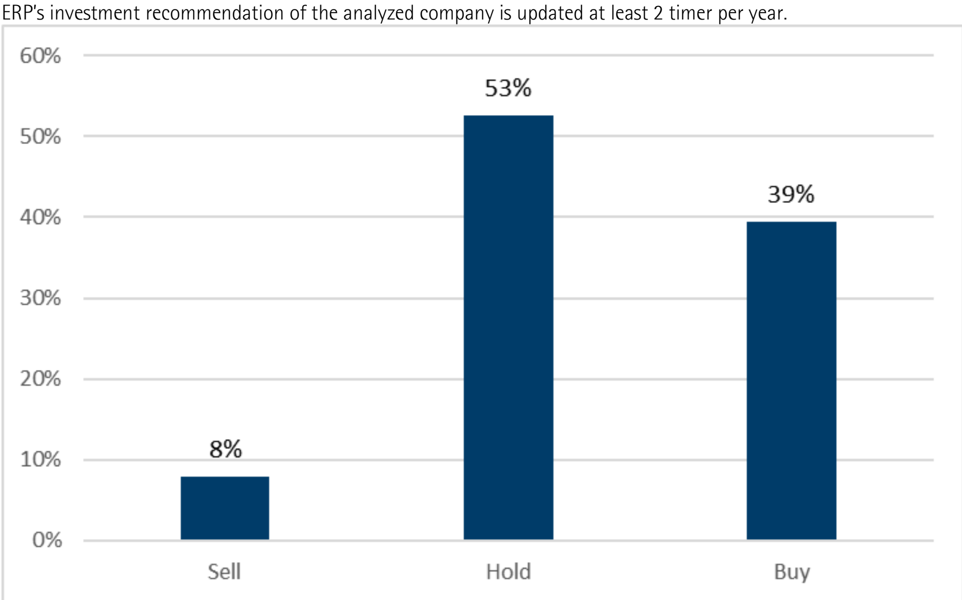
Important Disclosures

Evli Research Partners Plc ("ERP") uses 12-month target prices. Target prices are defined by utilizing analytical techniques based on financial theory including (but not limited to) discounted cash flow analysis and comparative valuation. The selection of valuation methods depends on different circumstances. Target prices may be altered on the basis of new information coming to light in the underlying company or changes in interest rates, changes in foreign exchange rates, other securities prices or market indices or outlook for the aforementioned factors or other factors that may change the conditions of financial markets. Recommendations and changes by analysts are available at Analysts' recommendations and ratings revisions.

Investment recommendations are defined as follows:

Target price compared to share price	Recommendation
< -10 %	SELL
-10 – (+10) %	HOLD
> 10 %	BUY

ERP's investment recommendation of the analyzed company is updated at least 2 timer per year.



The graph above shows the distribution of ERP's recommendations of companies under coverage in 1st of February 2019. If recommendation is not given, it is not mentioned here.

Name(s) of the analyst(s): Salokivi

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