Sanoma

Comprehensive report

5/2020

Inderes Corporate Customer

Translated from the FI original by the translation agency Delingua

inderes.

Learning's strong value creation capacity in a key role

We reiterate our Increase rating and raise our target price to EUR 9.5 (prev. EUR 9.0). In 2019–2020, Sanoma has implemented significant M&A transactions, as a result of which the focus of the company's value creation has switched to the defensive and highly profitable Learning business with stable growth prospects. Although the media sector is struggling with the effects of the coronavirus in the short term, the media business will become more stable and profitable in the long term with the increasing digital subscription revenues. In our view, Sanoma will recover from the coronavirus-related shock with moderate losses, and the expected yield of the share is attractive considering the long-term potential, the normalised result and the strong dividend flow.

The focus of value creation has switched to the most interesting areas for investors

In the last 12 months, Sanoma has carried out several significant M&A transactions (divestment of the Dutch media business, Iddink, Alma Media's regional newspapers) as a result of which the focus of Sanoma's value creation has switched to the profits in the areas most interesting to investors, learning and digital media contents. According to our estimate, these highly predictable, scalable and profitable business operations with reasonable growth prospects currently constitute approximately two thirds of Sanoma's operative result. Roughly 30% of Sanoma's net sales is still created by the revenues of the print media business, which is regressing as a result of the structural change. This slows down the development of the company's net sales, even though the digital subscription revenues and learning services are on the rise. To counter the pressure arising from the structural change, Sanoma has continued to make its operations more efficient and increased its activity – backed by a strong balance sheet – with regard to M&A that complement the value chain of the highly synergic and core operations.

Looking beyond the coronavirus, growth and profitability are slightly on the rise

Sanoma's short-term prospects are two-part: on the one hand, the coronavirus shock is weighing heavily on the 2020 ad sales and event income; on the other hand, Learning continues its strong and highly profitable growth. Looking beyond the coronavirus, we predict that the print media revenues – that currently form a little less than 30% of the media business net sales – will continue their approximately 5% fall, driven by changes in media consumption and the digitalisation of advertising. This being said, the learning material and digital learning platform revenues that currently comprise just under 40% of Sanoma's net sales will continue their steady growth, supporting profitability at the Group level. The digital revolution is also underway in the learning sector but the changes are gradual and Sanoma's prospects of growing its revenues are supported by inorganic growth as well as improvements in efficiency. Reflecting this overall view, we predict that Sanoma's net sales will increase by 17% in 2020. We expect profitability to be under pressure in the media business operations, and our prediction for the 2020 operational EBIT % (excluding PPA depreciations) is 14.3% (2019: 14.8%). In 2021, we expect the net sales to grow by 9% thanks to the resurgent economy, which in turn boosts profitability, which will increase to 15.6%.

Expected yield to rise to a good level

On a result basis, Sanoma's valuation level for the next few years is conservative (20–21e P/E adj. 12–14x), and the share provides investors with a solid expected yield (approx. 6%) via dividends. Once the coronavirus crisis blows over, we project that the strong revenue growth component and long-term valuation view ('sum of parts' and DCF EUR 10–11) will boost the share. We also see as a positive option potential new acquisitions, for which Sanoma has a financing reserve of approx. MEUR 300 available.

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Recommendation and target price

Increase
(prev. Increase)

EUR 9.50
(prev. EUR 8.50)

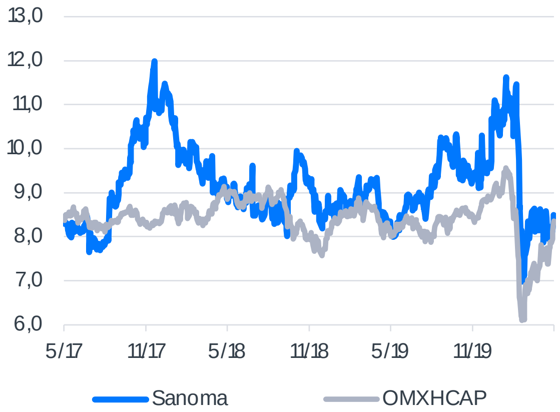
Share price: EUR 8.55
Potential: 11.1%

Key indicators

	2019	2020e	2021e	2022e
Net sales	913	1065	1158	1173
growth %	-3.1%	17%	9%	1%
EBIT adj. without PPA	135	152	180	187
EBIT % adj.	14.7%	14.3%	15.6%	16.0%
Net profit	61.4	83.4	109.8	117.5
EPS (adj.)	0.49	0.62	0.71	0.75
P/E (adj.)	19.4	13.8	12.1	11.3
P/B	2.9	2.6	2.4	2.3
Dividend yield %	5.3%	6.1%	6.3%	6.8%
EV/EBIT (adj.)	18.9	14.3	11.2	10.1
EV/EBITDA	9.3	6.4	5.2	5.0
EV/Net sales	2.6	1.7	1.5	1.4

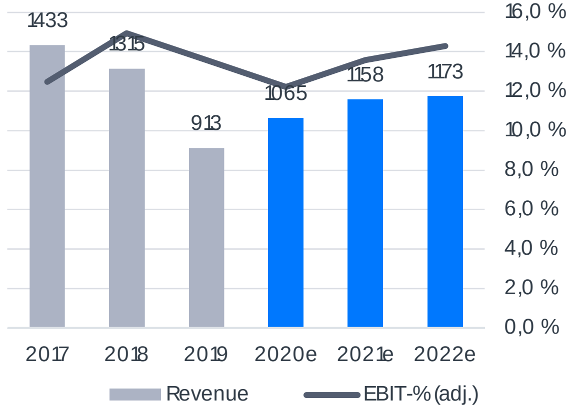
Source: Inderes

Share price



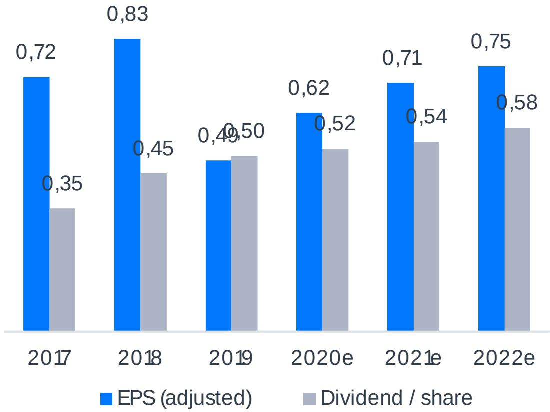
Source: Thomson Reuters

Net sales and EBIT margin (%)



Lähde: Inderes

Earnings per share and dividend



Lähde: Inderes

MCAP
1,389
MEUR

EV
1,860
MEUR

Dividend
6.1%
2020e

EV/EBIT (adj.)
11.2
2021e

Value drivers

- Digital revenue and service growth
- Better cost-effectiveness and net sales structure due to the growth in Learning
- Improved cash flow and financial position
- Mergers & Acquisitions (M&A)

Risk factors

- Accelerated decline of print media
- Weaker competitive position, especially compared to global competitors
- Failed M&A
- Risk of economic fluctuation
- Political risks
- Risks introduced by the coronavirus pandemic

Valuation

- Good organic yield growth prospects
- Strong operative cash flow and balance sheet enable healthy, increasing dividend yield
- Neutral valuation coefficients
- The ‘sum of parts’ calculation and cash flow model that describe the longer-term potential indicate clear room for increase

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Sanoma in brief

Comprising two independent business units, Sanoma Group is a leading Finnish media company and one of the leading providers of learning materials and methods in Europe.

MEUR 913
Net sales 2019, -1% vs. 2018 comparably

14.8% (11.2%)
Adjusted EBIT margin without procurement cost depreciations (EBIT margin), 2019

37%/54%
Learning's share of net sales and operational EBIT excl. PPA, 2019

27%
The percentage of cyclical advertisement revenues of the net sales, 2019

2013–2015

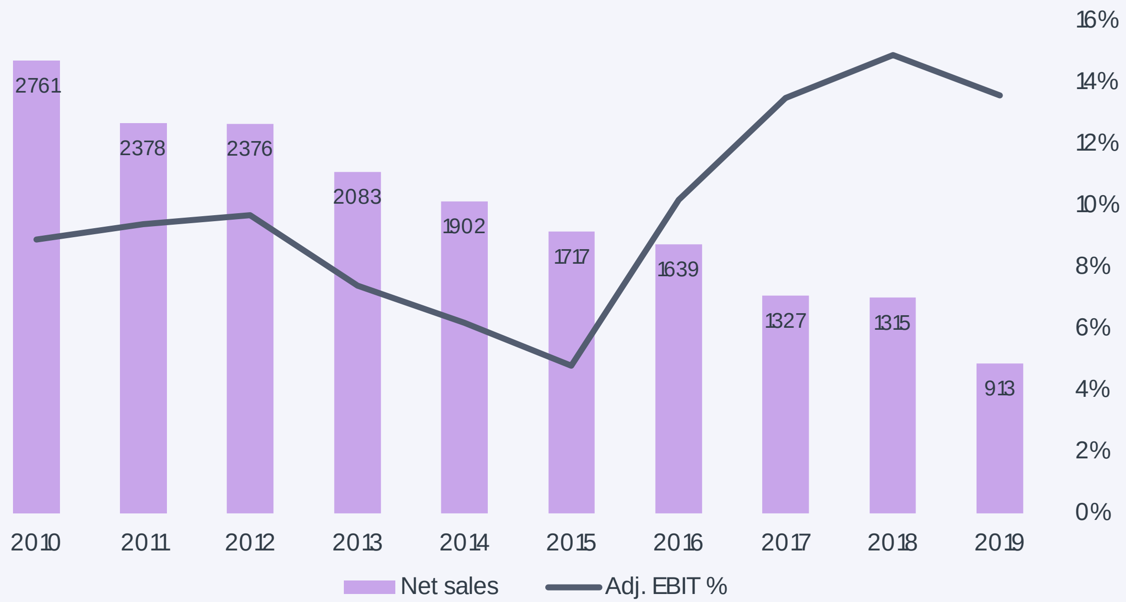
- The acceleration of the media's structural change, the muted economic environment as well as the costs of structural change are placing a burden on the revenue and profitability of Sanoma's media operations.
- The first write-down of the SBS acquisition
- Learning is developing strongly
- The company's leverage is growing high

2016–2018

- Focus on three business units and the divestments of unprofitable, non-synergic business operations
- Large-scale measures to improve the effectiveness of business and administration
- Profitability begins to improve strongly
- Improved cash flow, decreased leverage and a significantly improved balance sheet

2019–

- Continued focus with the company divesting the Dutch and Belgian media business units and strengthening its grip on Finland via the acquisition of Alma's regional newspaper operations
- Learning acquisitions that reinforce and complement the value chain
- Increase of the proportion of recurring net sales
- Strong balance sheet and cash flows, enabling M&A



Source: Inderes, Sanoma

Sanoma's business model 1/3

Media and learning solutions

Comprising two independent units, Media Finland and Learning, Sanoma Group operates in the media and learning sectors. While the Group currently has media units only in Finland, it has learning business units in ten countries.

In 2019, the net sales of the Group's continuous operations was MEUR 913 and the operational EBIT excl. PPA (hereinafter operational EBIT) was MEUR 135 or 14.8% of the net sales. Sanoma is a market leader in the Finnish media market as well as the learning material and solution markets of the Netherlands, Poland, Finland and Belgium. The company's well-known brands and products include Helsingin Sanomat, Iltasanomat, Nelonen, Ruutu, Donald Duck and the gamified learning platform Bingel. All in all, Sanoma's portfolio comprises dozens of leading media, digital service and learning brands.

Two independent business units

The **Learning** business comprises the sales revenues of printed, digital as well as hybrid learning materials and solutions. In 2019, the business unit constituted 37% of the Group's net sales and 51% of its operational EBIT.

Sanoma's biggest business unit by net sales, **Media Finland**, is the leading media company in Finland. The segment's revenues primarily comprise the content and advertising revenues of the newspaper, news and magazine media, the advertising and subscription revenues of TV, radio and the related online services as well as revenues from other services, such as the festival business units. In 2019, Media Finland constituted 63% of the Group's net sales and 49% of its operational EBIT.

In addition, the company reports the Group's other expenses not allocated to business segments under the Other Companies and Eliminations segment.

Four revenue components

Sanoma's business model can be divided by revenue type into four main components, which differ from each other in terms of the continuity of revenue, customer type and cyclicity.

1. **The media content revenue** (in 2019: approx. 26% of Sanoma's net sales) comprise the subscription and single-copy sales revenue of printed newspapers and magazines (such as HS and Donald Duck) as well as online news and entertainment media services (such as HS.fi and Ruutu). To a significant degree, the content revenue net sales comprises recurring revenues, the percentage of which of Sanoma's net sales is approximately 21%, whereas the corresponding percentage of single-copy sales is only 5%. The main customer target group of content revenue comprises consumer customers.

2. **The media advertising revenue** (in 2019: approx. 27% of the net sales) comprise the advertising revenue generated by newspapers, magazines, TV, radio, the related online services as well as the online marketplaces (e.g. oikotie.fi). The share of digital media of the advertising revenue has increased to roughly 75%; therefore, it plays a clearly bigger role than print media. The main customer target group of advertising revenue comprises corporate customers. Advertising revenue trends are cyclical by nature because companies' investment in advertising is typically strongly dependent on their overall economic development.

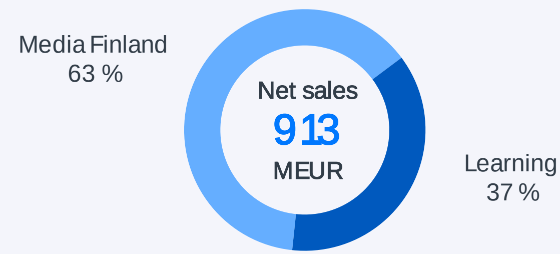
Sanoma's business structure, 2019

Sanoma Group
Net sales of MEUR 913, EBIT (adj. excl. PPA) MEUR 135

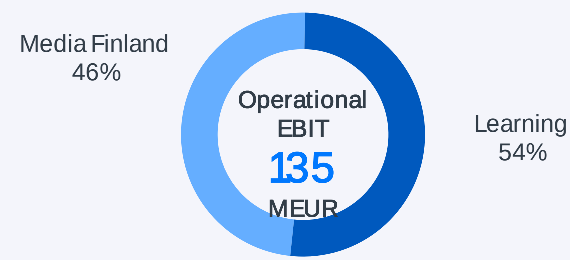
Media Finland	Learning
Net sales MEUR 577 EBIT* MEUR 69 EBIT % 11.2%	Net sales MEUR 337 EBIT* MEUR 73 EBIT % 19.9%
• Newspapers • Online media • TV & radio • Magazines • Festivals • Other services	• Learning materials • Digital learning platforms

* Operational EBIT excl. PPA depreciations

Net sales distribution, 2019



EBIT distribution, 2019



Sanoma’s business model 2/3

2. **Learning revenue** (in 2019: approx. 37% of the net sales) comprises in full the revenues of the Learning segment’s learning materials and digital learning platforms. The main customer target group of the Learning revenue comprises the public sector.

   The Learning revenues are not tied to the general economic development in the short term. However, they are subject to some fluctuation linked to terms and curricula. The annual Learning revenues are strongly concentrated on Q2–Q3, which also results in strong seasonal fluctuation in Sanoma Group’s net sales. In addition, the annual Learning revenues may vary wildly at the annual level because the demand for learning solutions is strongly dependent on the curriculum reforms that typically occur every 5–10 years in individual education markets.

4. **Other revenue** (in 2019: approx. 10% of the net sales) consists of the Finnish festival operations, marketing services, corporate publications as well as books and printing services. Although other revenue’s main customer target group is businesses, the majority of the income of the festival operations that typically comprise approx. 40% of the other revenue comes from consumers.

Structural trends have a material impact

In addition to the normal demand drivers, Sanoma’s revenue trend is guided by several diverse structural trends of different magnitude.

The structural trend that most affects Sanoma is the regression of print media resulting from the digitalisation of media consumption that strongly affects both the development of print media content revenues and, especially, print media advertising. The share of print media revenue of Sanoma’s net sales is around 30%. According to our estimate, of this, content revenues constitute approximately 75%, print media advertising approximately 20% and other revenues approximately 5%.

A trend contrary to that of the print media is the structural growth of digital media revenues. In our estimate, the share of digital media revenue (excl. linear TV & radio) of Sanoma’s net sales is around 15%. We estimate that digital advertising makes up approximately 55% and digital content revenues approximately 45% of this.

The structural trends also affect the growth of learning, TV & radio and other revenues, but more widely than those of print media. TV & radio makes up approx. 12%, Learning 37% and other revenues, including festivals and marketing services, approx. 6% of Sanoma’s net sales.

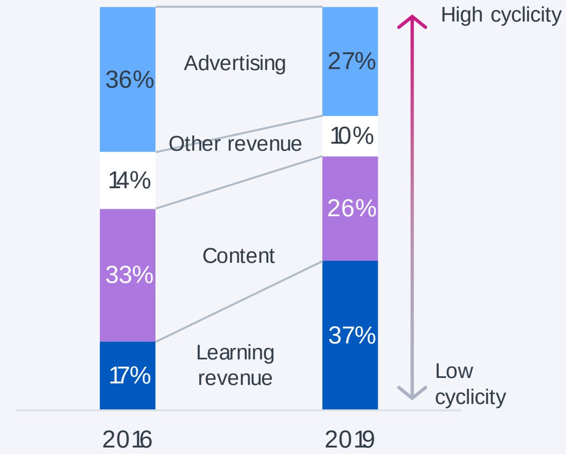
Overall risk profile of Sanoma’s business model is moderate

In our opinion, the overall risk profile of Sanoma’s business model is moderate (see the graph on the next page).

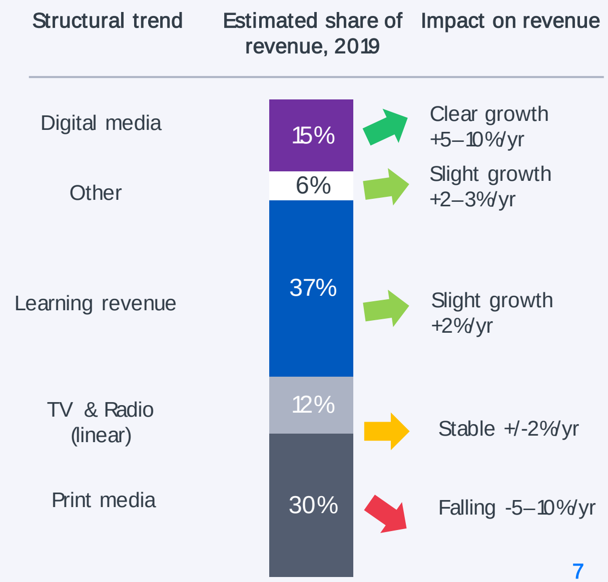
The business model’s risk level is specifically reduced by the moderate share of cyclical revenue, high percentage of recurring and predictable revenue, strong market position as well as foreseeable operational cash flow.

The business model’s risk level is primarily increased by factors related to the revolution of the media sector that strongly reduce the demand for print media, undermine Sanoma’s pricing power and reduce the scalability advantages of the print media business operations.

Sanoma’s revenue distribution, 2019



Estimated effect of structural trends on Sanoma’s revenue



Sanoma's business model 3/3

High percentage of easily foreseeable revenue

The percentage of Sanoma's net sales of business operations with revenues from recurring subscription streams is approximately 64%, and they comprise very stable and predictable learning revenue and content subscription sales.

The percentage of advertising revenue – which is heavily dependent on consumer demand and economic cycles – of Sanoma's net sales has decreased markedly as a result of the restructuring taking place in the last few years. The percentage of advertising revenue of the Group's net sales is currently approximately 27%, while in 2016 it made up 36% of the net sales.

With the percentage of advertising revenue decreasing, recurring subscription sales-based content revenues have taken a strong foothold and they currently constitute approx. 19% of the net sales. The share of learning revenue subject to stable and predictable demand has also increased to 37% (in 2016: 17%). The share of non-recurring content revenue (single copy) has dropped very low, to approximately 4%. In addition, the company's expansion to new business operations in value chains parallel to the core businesses is evident in other revenues, which constitute 8% of the net sales. It should be noted with regard to 2022 that the coronavirus pandemic will reduce the net sales or Sanoma's festival operations (in 2019: MEUR 35 or approx. 4% of the net sales) to the zero level for all practical purposes.

Global competition and the regression of print media reduce pricing power

Sanoma holds a strong market position in its own fields of specialisation, especially the Finnish media market. Traditionally, this has guaranteed Sanoma's strong pricing power. However, the reduced accessibility of the print media, the fragmentation of media consumption as well as the competitive pressure introduced to a large degree by Google and Facebook have weakened the advertising pricing power of local media companies. According to our estimate, the speed of change is levelling out, with larger media companies improving their technological solutions and winning a market share from small domestic operators.

Print media's scale advantages are on the decline but digital provides great scale advantages

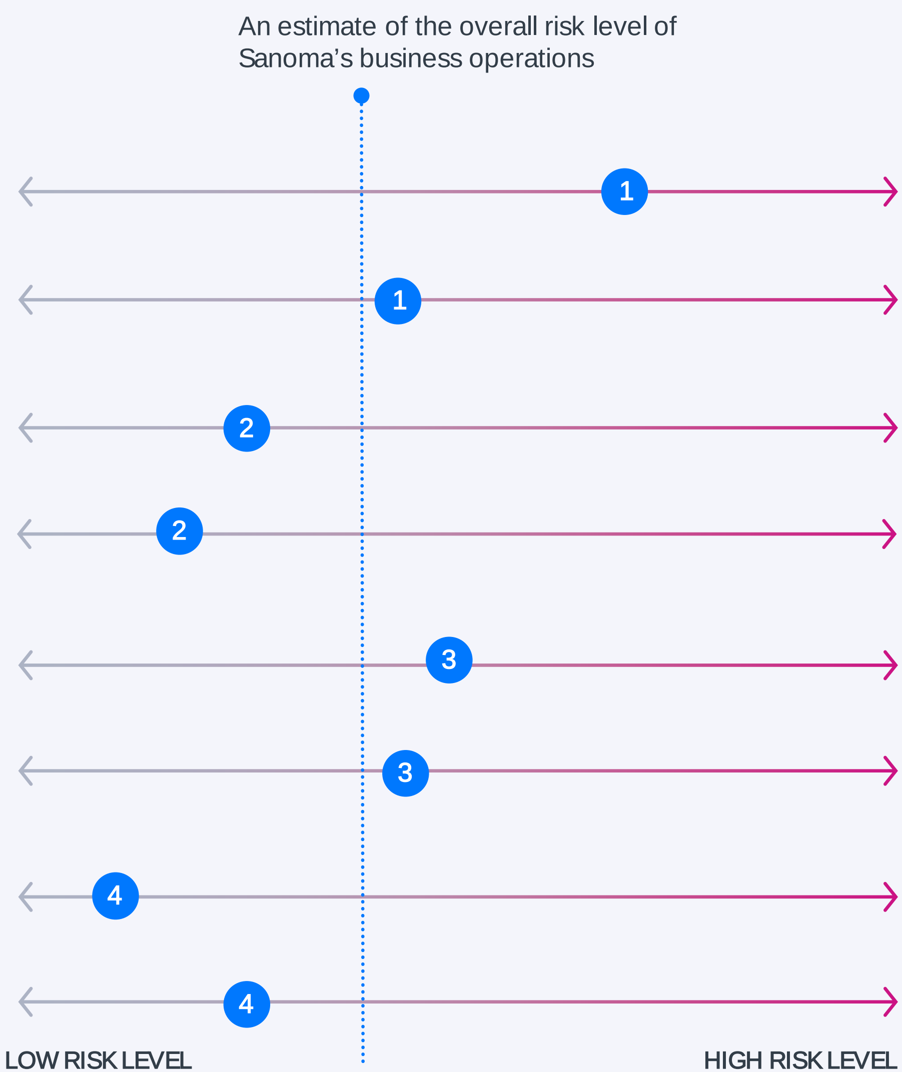
Typically of the newspaper, magazine and learning material business, Sanoma's cost structure is for all significant parts fixed. As a result of the regression of the print media, Sanoma's scale advantages with regard to the print media have, in our estimate, decreased. Subsequently, the company has been forced to continuously trim down its fixed costs and increase the efficiency of its operations.

That said, the scale advantages are much more pronounced in the strongly-growing digital revenues, where the relative profitability is better, compensating for the print media's diminishing profitability potential.

Strong operational cash flow and a moderate need for investment

Overall, the ability of Sanoma's business units to produce a cash flow is excellent for the following reasons: 1) the content and advertising revenue's cash flows are typically very front-heavy and they contain a lot of advance payments; 2) the Group's net working capital is negative; 3) the organic level of the business units typically ties up a low level of capital; and 4) there is little need to invest in material and immaterial commodities, with the exception of programme rights and product development investments.

Risk profile of Sanoma's business model



1 OPERATING ENVIRONMENT	The sector's rate of change	The sector is going through continual change driven by digitalisation and technological development.
	The company's developmental stage	Following a major structural change, Sanoma has entered a stable development stage and holds a strong market position, with a relatively low percentage of print media (approx. 30%)
2 NET SALES	Market cyclicity	The portion of cyclical advertising revenue is relatively low, roughly 30%. Learning revenue streams (approx. 40%) and subscription revenues (approx. 25%) are stable in nature.
	Dispersion and continuity of net sales	A highly dispersed business operation and customer portfolio and a high percentage of recurring revenues.
3 PROFITABILITY	Pricing power	A strong market position in the core operations, but the digital revolution of the media sector as well as global competition reduce pricing power.
	Cost scalability	Print media's scale advantages are on the decline but digital operations are highly scalable and increase the overall profitability.
4 CAPITAL STRUCTURE	Operational cash flow	Strong operational cash flow and clearly negative net working capital.
	Capital intensiveness	Low working capital investments. The investments primarily comprise the intellectual rights and activations pertaining to TV, magazines and learning materials as well as the business value generated by acquisitions.

Source: Inderes

Sanoma's strategy

No specific Group-level strategy

Sanoma does not have a specific Group-level strategy; its strategy comprises the individual strategies of its independent business units. In our view, it is natural not to have a Group-level strategy as the business models, markets and competitive fields of Sanoma's different units are drastically different from each other, without practically any operational synergies between them. Furthermore, in the media sector where the landscape shifts quickly, rigid long-term Group-level strategies could even impair Sanoma's competitiveness.

Group-level trends

In the last few years, the development of Sanoma Group has been steered by trends comparable to strategic goals. In 2018–2019, the company completed a significant structural change started in 2015. During this stage, Sanoma focused on its market-leading core businesses, simplified its business structure and implemented large-scale cost-saving and improvement measures. Despite the decreasing net sales, the development stage can be considered successful as it markedly improved the company's profitability as well as its cash flow and, at the end of it, the company met its financial targets in terms of dividend growth, indebtedness and solvency.

In our opinion, Sanoma's strategic focus in the next few years will be on organic growth that utilises the scalability of its core businesses, cost management as well as improving the company's cash flow. In addition, the growth is expedited via inorganic growth.

Acquisitions an important part of strategy

Acquisitions play an important role in improving Sanoma's financial performance and business development. Sanoma needs acquisitions to increase its net sales, reinforce its value chain, ensure the continuous improvement of its performance as well as its economies of scale and to replace the fading profits of its print media. Acquisitions are used to steer the use of resources to a more efficient direction.

Sanoma's financial position and cash flow have improved significantly in the last few years, so Sanoma has the capacity – backed by cash flow financing and liabilities financing – to carry out acquisitions worth approximately MEUR 300. In addition, the Oikotie unit, which is under strategic review, will potentially liberate significant additional ammo for acquisitions. According to Sanoma, it has a clear array of potential targets, and acquisitions can be expected in the next 12 months.

In the next few years, acquisitions by the business units will in our estimation be specifically focused on the Learning segment, where the aim is to penetrate new markets both geographically and in terms of service provision as well as improve the economies of scale and the market position. We estimate that Media Finland will be active in the next few years in relatively small-scale acquisitions that will strengthen the value chain and the economies of scale.

Sanoma's management has highlighted that the company will use acquisitions to unearth important synergic benefits, new market potential and/or new scalable services. In our view, it is therefore unlikely that Sanoma will take part in large-scale market consolidation in the short term.

Financial targets

Sanoma set the following long-term financial targets in 2016:

1. Growth and profitability: A growing dividend corresponding to 40–60% of the annual free cash flow.

2. Leverage: The ratio of net debt and the adjusted operated profit is below 2.5x.

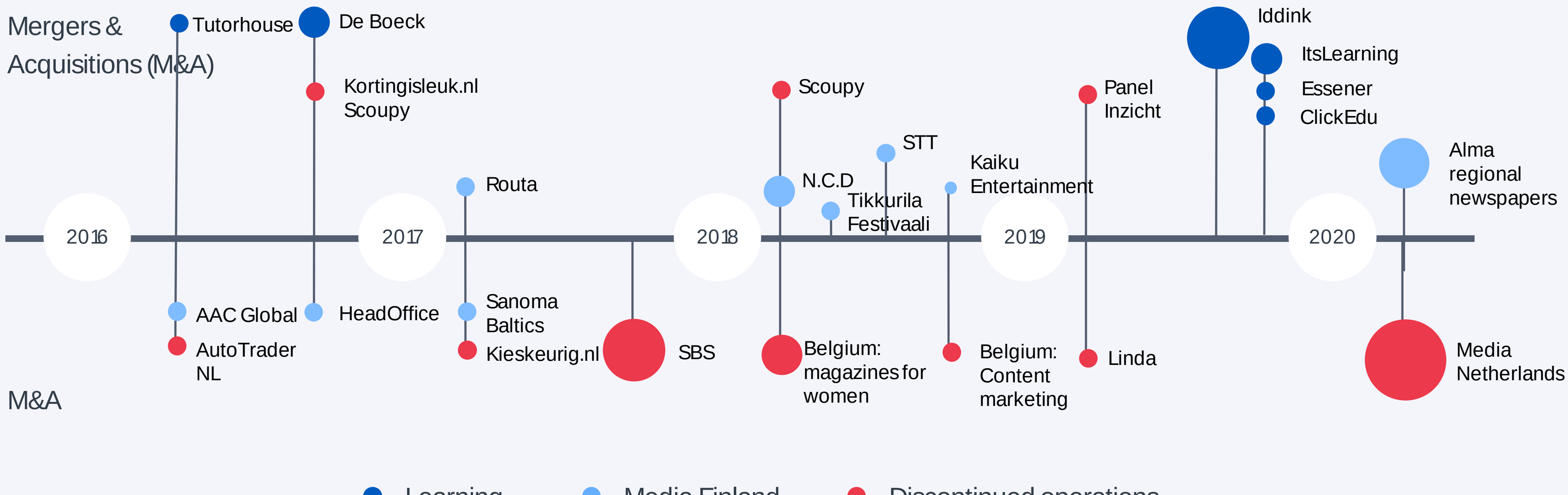
3. Solvency: An equity ratio of 35–45%.

In the light of the latest reported figures (Q1 2020), leverage is above and, correspondingly, equity ratio is below the levels indicated by the long-term financial targets. However, we expect the situation to right itself with the sale of Media Netherlands, confirmed in April. Our forecasts expect the company to reach the level indicated by the targets by the end of the year.

In its dividend policy, Sanoma has specifically highlighted dividend growth, which is tied to the development of free cash flow. Although we believe that Sanoma will hold on to this target in the long run, we expect the company's dividend to rise only slightly in 2020 due to the uncertainty arising from the coronavirus pandemic.

All in all, we consider Sanoma's financial targets to be relatively moderate, with an emphasis on stable development. They are a good fit with Sanoma's current business profile, where the regressing traditional media continue to generate a healthy cash flow and acquisitions, growing digital revenues as well as improvement measures increase revenues. The company has also provided the segments with their own financial targets, which will be discussed in separate sections.

Sanoma’s acquisitions in 2016–2019 and the segments’ M&A strategy



Source: Sanoma

The business units’ M&A strategy

Media Finland

- The importance of M&A is complementary
- The focus of M&A is on complementing the value chain and increasing growth
- Primarily small acquisitions in the areas with high synergies with the core operations
- Establishing partnerships and consolidation possible if the opportunities present themselves
- Divestments may be carried out to develop the portfolio

Learning

- The importance of M&A is high
- M&A target areas include basic education learning solutions (K12) and the related markets
- Increasing the economies of scale and market shares in the current markets’ core operations
- In the value chain, expansion in the current market areas
- Geographical expansion to new markets in the core operations

Source: Inderes

Sanoma's strategic development

2015–2017

Turnaround and structural change stage

- Focus on improving profitability and cash flow as well as concentration on the core operations
- Divestment of the TV operations in the Netherlands
- Large-scale improvement programmes in the Media Finland and Media Netherlands segments and Group functions
- Financial restructuring

2018–2019

Stabilisation of the core operations and becoming active in M&A

- Focus on improving profitability and cash flow
- The sale of the last non-synergic, non-core business units (the Belgian and Dutch media business units)
- Small "smart" acquisitions of media operations as well as the important Iddink M&A in the Learning business unit
- The net sales development was stabilised but the inorganic growth is slightly negative
- Learning implemented the "High Five" programme aimed at improving efficiency

2020–

Stable profitability, improved cash flow and synergic M&A

- Core operations at a stable development stage
- The structural revolution of media continues
- Acquisition of Alma Media's regional newspaper operations
- Expansion of the geographical and service portfolio in Learning
- Development of the business portfolio via divestment

Strategic trends

Realised

- Business structure lighter, more focused and more profitable
- The net sales fell by approx. 30% as a result of the restructuring
- Profitability rose to a healthy level across the business units (2015: adj. EBIT % approx. 5% -> 2019: adj. EBIT % approx. 15%)
- The company's net debt decreased significantly
- Thanks to the improved cash flow and performance, the dividend per share increased from EUR 0.10 to EUR 0.5

Near future 1–2 years

- The coronavirus pandemic is creating challenges for the festival business and ad sales but it boosts the entertainment service consumption
- As a result of the coronavirus and the structural change of media, the organic net sales trend is negative
- However, thanks to acquisitions, the overall net sales is clearly positive
- Steady profitability improvements
- The gradual improvement of cash flow and business efficiency

The next 5 years

- Management of the structural change of media and the gradual improvement of profitability with the ongoing switch from print media to digital consumption
- Learning, digital services, festivals and M&A as drivers of growth
- According to Inderes's assessment, both Sanoma Media Finland and Learning have grown to a significant size and can be separated into independent companies within the next five-year period

Source: Inderes

Sector review – Learning 1/2

Structural drivers of demand linked to educational reforms and improved efficiency

In our view, the learning sector's prospects and demand are influenced by three key drivers: the structural change of demand driven by digitalisation, the ongoing educational and education system reforms as well as the need to make learning results and resources more effective.

The structural change of demand driven by digitalisation has also affected the learning market for quite a long time. However, as a result of the slow rate of change, the change taking place in curricula and education systems as a whole has been significantly slower, more predictable and more controlled than in the media market. Digitalisation is reflected in the learning market primarily in the declining use of printed learning materials and, at the same time, the higher demand for digital learning solutions, new business and pricing models as well as competitors offering new purely digital solutions.

The primus motor of the learning market are still country-specific curriculum and education system reforms that typically occur in 5–10-year cycles. While the changes in these cycles dramatically affect demand in the short term, the long-term trend growth is slow.

The third driver that steers and increases demand in the learning market in the long run is the increasing need to improve the learning results and, specifically, the need of the private education sector to improve the efficiency of training investments. This provides learning companies with opportunities for business growth linked to both basic education and digital learning platforms.

Key trends of the learning market

In our opinion, the key trends affecting the learning market are:

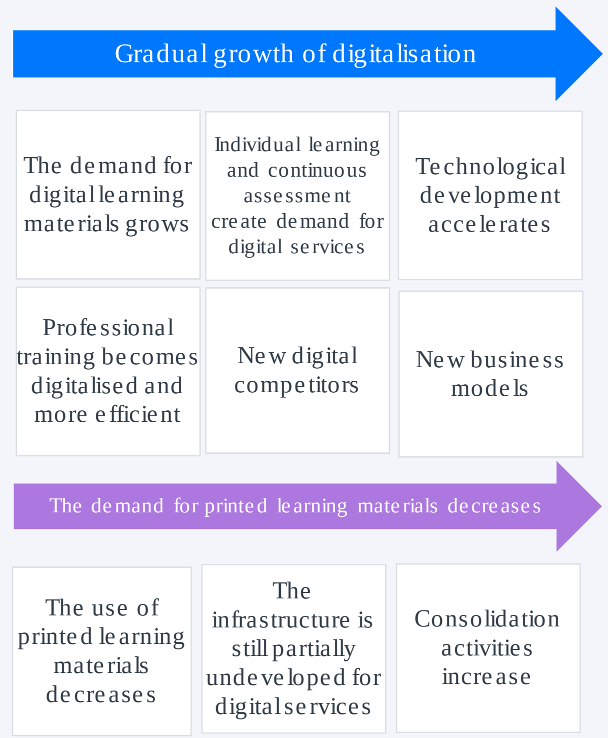
- The market share of learning solutions that combine printed and digital learning materials and purely digital learning solutions is growing.
- Individual learning and the continuous assessment of learning are becoming more commonplace. This shapes the demand for learning solutions and increases the demand for digital services, specifically.
- The requirements of educational methods will become stricter and the rate of change will become faster, increasing the need for solutions that support teaching.
- Professional learning solutions will become digital and their efficiency requirements will become higher.
- The number of competitors will increase with new digital operators, and the consolidation of traditional operators will continue.
- The sector will implement ongoing subscription fee-based business models.

According to our estimate, the switch to distance learning driven by the coronavirus pandemic has increased the demand for digital learning solutions, contributing to the gradual growth of digitalisation.

Learning material market prospects

While the share of the learning material market of the total costs of education in Sanoma's market areas is only about 3%, it still makes up the majority of the net sales for learning companies such as Sanoma. We estimate that this section of the market will grow slowly in the long term (+0–2%/year) because the use of printed learning materials will decrease and the age groups will diminish.

Key trends of the learning market



Sector review – Learning 2/2

With the digitalisation of learning materials and the teaching method reform, the market shares of digital solutions are being redistributed between the more competitive operators and the traditional operators concentrated on printed materials. In our estimate, Sanoma is well-positioned in this revolution as it has a comprehensive and well-developed digital solution portfolio and it holds a strong market position in its own focus areas.

Outlook for learning systems and platforms

The share of learning systems and platforms as well as administrative education systems of the net sales of learning companies such as Sanoma is still relatively small (approx. 10–20%) even though their costs are covered by the education budget allocated to administration, systems and development – which at approximately 15% of the total costs of comprehensive school education (K12) is normally far bigger that the learning material budget.

As a result of the above-mentioned trends as well as the larger market potential of the learning market, the long-term growth prospects of this sector are, in our view, clearly more positive (>5%/year) than those of the learning material market.

The competitive field mainly consists of local learning companies

The learning sector requires strong country-specific expertise, tailoring and competence as well as a comprehensive sales and distribution network. For example, in Finland, teachers have a high level of autonomy and freedom to choose the learning material format and solution they want, which spreads the decision-making process across a large group. Subsequently, the market entry threshold is extremely high, and competition mainly occurs between local operators. Furthermore, the number of operators in the sector is typically fairly small because in order for learning material publishing to be financially viable, it must be relatively large-scale.

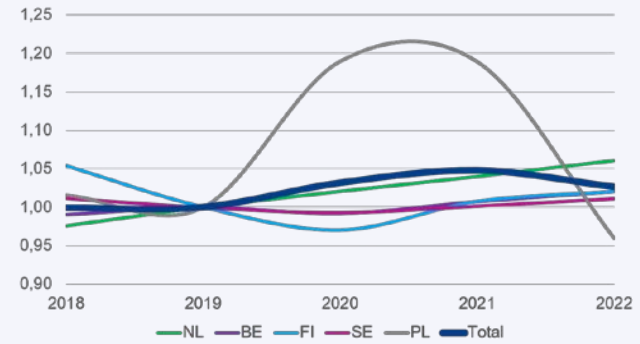
When it comes to digital platforms and applications, however, the competitive field is much more fragmented and global because competition there occurs more between different technologies than different contents and methods. Subsequently, the competition is not quite as dependent on familiarity with the local playing field. Nonetheless, according to the companies operating in the sector, the infrastructure at schools is still lacking, which slows down the adoption of digital materials.

Sanoma's main competitors in the field of publishing are Otava in Finland, Noordhoff and ThiemeMeulenhoff in the Netherlands, Plantyn and Pelckmans in Belgium, WSiP in Poland as well as Liber, Natur & Kultur and Gleerups in Sweden.

Noordhoff, Plantyn and Liber are owned by Infinitas Learning. ThiemeMeulenhoff is owned by Klett, a German company. According to Sanoma, all of the above individual, country-specific companies mainly operate solely on their home market and none of them has significant operations in several countries even if they had the same owner.

According to Sanoma, no major publishers of K12 materials have so far emerged as a competitor in any of the countries where Sanoma Learning operates.

Growth forecasts for the learning material market



Sanoma Learning 1/3

A steadily growing performer

In 2019, based on net sales (2019: MEUR 337/37% of Sanoma's net sales), Sanoma Learning was Sanoma's smaller segment but thanks to its higher profitability, based on EBIT (2019: operational EBIT %21.7%, operational EBIT MEUR 73/55% of Sanoma's operational EBIT), it was the larger segment.

The operations of the Learning segment comprise the sales revenues of printed, digital as well as hybrid learning materials and solutions. The main segment of the company's products and services is the so-called K12 segment, which covers first- and second-level education as well as vocational training.

Most of Learning's revenues come from the steadily growing basic education market

Most of Learning's revenues are generated by the steadily developing and highly predictable basic education learning material and learning solution market.

From the aspect of product and service type, approximately 55% of Learning's net sales constitutes content, which covers both printed and digital contents, 30% comprises material distribution, and the remaining 15% is evenly distributed between teaching platforms, administration platforms as well as test and analytics services.

Geographically, more than 90% of the Learning segment's business comes from markets where it has a comprehensive service portfolio and where it is historically the largest or second largest operator. Similarly, a materially smaller market constitutes markets where the company has – at least for the time being – a limited supply and which the company has entered only recently. In 2019, the Netherlands comprised 32%, Poland 28%, Belgium 17% and Finland 16% of the net sales. On the combined learning market of these countries plus Sweden, Sanoma's market share was 40.5% in 2019 (2017: 39.2%) according to Sanoma's own estimate. Less than 10% of Learning's net sales comes from smaller market shares in Sweden, Spain, Norway, Denmark, France and Germany.

Sanoma Learning's companies include Sanoma Pro and ITSL in Finland, Nowa Era in Poland, Van In in Belgium, Malmberg in the Netherlands, Sanoma Utbildning in Sweden as well as Bolster and Iddink in the Netherlands, Belgium and Spain. The strong market position of the segment's business units is based on the local companies' long history as learning material publishers, developers and distributors. For instance, Learning's Finnish unit, Sanoma Pro, has been publishing textbooks for over 130 years. Learning has also been historically able to increase its market share in connection with curriculum changes.

Financial targets and strategy

The long-term financial targets set by Sanoma for Learning include a 2–5% growth of comparative net sales as well as an adjusted EBIT of 20–22%, excluding PPA depreciations.

Learning mainly targets growth organically in connection with curriculum changes as well as with the increasing level of digitalisation. In addition, the segment continues to expand to new geographical areas and grow its technology and service offering.

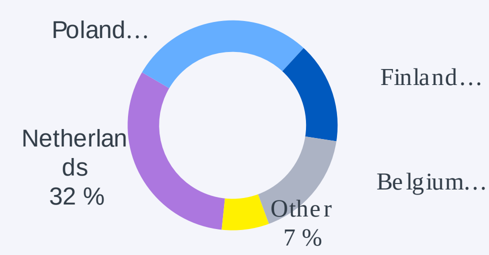
Learning in brief, 2019

MEUR 337 (2018: MEUR 313)
Net sales 2019

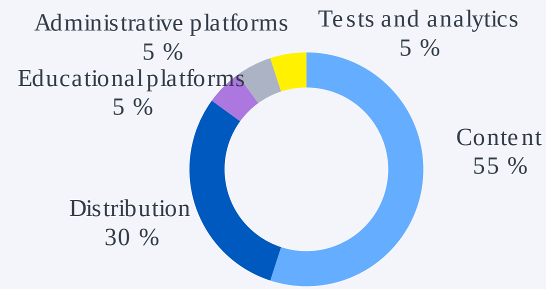
21.7% (2018: 20.3%)
Profitability, operational EBIT %

41% market share in 2019
Poland, Finland, Belgium, the Netherlands and Sweden

Net sales by area, 2019



Net sales by product line, 2019



Sanoma Learning 2/3

In our estimate, the curriculum reforms in the Netherlands and Poland as well as the drivers effective on the market will support Learning's growth targets in the medium and long terms. Occasionally, the variation in teaching cycles materially affects the segment's net sales trend. As an example, the end of the Polish curriculum reform – which has a positive effect in 2020 and 2021 – will have a negative growth effect from 2022 onwards. Mirroring this growth outlook, Learning's growth rate is significantly influenced by geographical expansion to new markets as well as the increase of the service portfolio in the current markets.

We estimate that Learning will keep trying to strengthen its hold, especially on the digital learning platforms in the different markets, because this position is strategically attractive due to the stable nature of revenue (compared to the cyclical nature of content arising from a curriculum reform). We also estimate that purchases will be more permanent in the platform segment because the threshold for changing platforms is high due to the high cost involved, whereas changing learning materials is easier when the curriculum changes. The company can perform expansion like this by introducing platforms already owned by it to markets where the level of digitalisation is rising or inorganically by acquiring strong platforms already prevalent in these markets. And so, in our view, the emphasis of Sanoma's M&A strategy will be, above all, on expanding Learning.

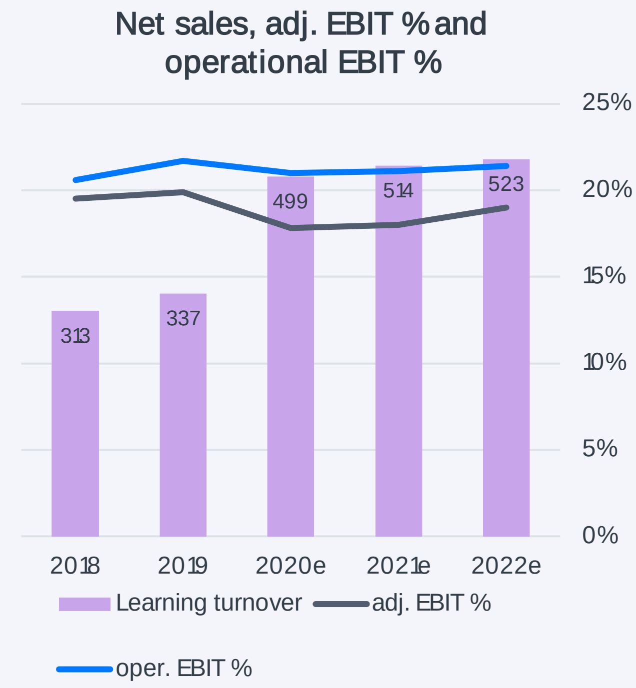
With regard to profitability, we expect the segment to develop in a relatively stable manner in the short and medium terms in accordance with the financial targets (operational EBIT % 20–22%), with curriculum reforms and the effects of efficiency programs reflecting in profitability, for example. In the long term, we anticipate increasing digitalisation and a larger scale to boost profitability, keeping it on a slight upward curve.

Forecasts

Our forecasts are based on the assumption that Sanoma will be able to maintain or improve its market share in all of Learning's essential markets. We project the net sales of the Learning segment to grow strongly in 2020, specifically in the Netherlands as a result of the acquisition of Iddink, but also in other regions. In addition, we expect the net sales to increase in Poland as a result of the curriculum reform, whereas in Finland, the corresponding driver will slow down growth. Therefore, we anticipate that the 2020 net sales will increase by 48% to MEUR 499 (2019: MEUR 337).

In 2021, we expect the growth of the net sales to slow down, but it will still be boosted by the curriculum reform in Poland. This is why we anticipate that the net sales will increase by 3% to MEUR 514 in 2021. According to our projection, the growth will slow down once again in 2022 to slightly below 2%, with the net sales rising to MEUR 523.

We forecast Learning's 2020 operational EBIT to grow by 43% to MEUR 105 (2019: MEUR 67) reflecting inorganic growth and its operational EBIT % to fall to 21.0% (2019: 21.7%) reflecting the change in the distribution of net sales. On the other hand, we expect the reported net sales to grow at a decidedly slower rate, as we expect the PPA depreciations resulting from M&A to notably increase this year.



Profit and loss account	2018	2019	2020e	2021e	2022e
Net sales	313	337	499	514	523
Operational EBIT	64.6	73.1	104.5	108.5	111.8
Adj. EBIT	61.2	67.2	88.5	92.5	99.3
EBIT	*56.1*	*55.1*	*85.6*	*90.5*	*97.3*
Non-recurring items	-5.1	-12.1	-2.9	-2.0	-2.0

Growth and profitability	2018	2019	2020e	2021e	2022e
Net sales growth %	*-2.1%*	*7.6%*	*48%*	*3%*	*2%*
Operational EBIT growth %		14%	43%	4%	3%
Operational EBIT %	20.6%	21.7%	21.0%	21.1%	21.4%
Adj. EBIT %	19.5%	19.9%	17.8%	18.0%	19.0%
EBIT %	17.9%	16.3%	17.2%	17.6%	18.6%

Sanoma Learning 3/3

We foresee that in 2021–2022, the operational EBIT will grow by roughly 4–7% and the operational EBIT margin will be 21–21.5%. We foresee that, in the long-term forecast period extending to 2025, the net sales will grow on average by 2%, excluding M&A, and the operational EBIT margin will be approx. 21% and at a level corresponding to the company's financial targets.

In our view, a positive risk to our projections are acquisitions that accelerate revenue growth. Negative projection uncertainty is primarily brought by curriculum cycle changes, the effects of improvement measures as well as non-recurring items.

Learning valuation

When specifying the segment's value, we use as a reference value the 2020–2021 EV/EBIT and EV/S coefficients of control companies because there is some uncertainty pertaining to the 2020 projections resulting from the coronavirus pandemic.

We have identified 12 listed control companies for the Learning segment but, because of some operators' weak performance and different development stage, their valuation as a whole does not currently work as a relevant yardstick for Learning. In our estimate, of the control companies, Pearson, John Wiley & Sons Inc and Wilmington are most suitable for the valuation comparison, and we have bracketed Learning's acceptable valuation coefficient based on the average EV/EBIT coefficients for 2020 and 2021, which are 15x and 12x. We deem this valuation bracket absolutely justified considering Learning's business model and profitability potential. Based on our projections regarding Learning's 2020 and 2021 operational EBIT (excluding PPA depreciations) as well as the coefficients of the control companies, Learning's value will be approx. MEUR 1,300–1,567.

In our opinion, Learning's valuation may also be well compared to the valuation coefficients of the Iddink M&A. The adj. EV/EBIT excluding PPA depreciations coefficient for Sanoma's acquisition of Iddink was 12.4x. We project that Learning's operational EBIT for 2020 will be MEUR 88.5, in which case the M&A valuation coefficient would indicate that Learning's company value is approx. MEUR 1,080. Taking into account Iddink's smaller size category as well as Learning's more comprehensive business portfolio, we think that it is reasonable to accept a higher valuation coefficient for the Sanoma Learning entity than the valuation of the Iddink acquisition.

Therefore, Learning's value is MEUR 1,322 calculated on the basis of the methods we have used. Keeping this in mind, Learning's valuation has increased significantly from the previous comprehensive update (2019 valuation: MEUR 896). This has been especially influenced by our profit forecasts that have increased as a result of Learning's acquisitions and increased efficiency.

Learning peer group

Control companies	EV	EV/EBIT		EV/S	
Company	**MEUR**	**20e**	**21e**	**20e**	**21e**
Bloomsbury Publishing PLC	175	9.9	17.1	0.9	1.1
Houghton Mifflin Harcourt Co	727			0.6	0.6
Cengage Learning Holdings II Inc	2598				
Pearson PLC	5194	13.4	11.1	1.3	1.2
Scholastic Corp	770		53.0	0.6	0.5
K12 Inc	878	35.1	19.3	0.9	0.9
John Wiley & Sons Inc	2707	17.8	17.1	1.6	1.6
Wilmington PLC	182	15.1	8.2	1.5	1.4
Koninklijke Brill NV	40				
2U Inc	2125			3.3	2.8
Rosetta Stone Inc	395			2.3	2.1
Chegg Inc	6961	55.2	40.8	14.0	11.4
Average		**24.4**	**23.8**	**2.7**	**2.4**
Median		**16.4**	**17.1**	**1.4**	**1.3**

Sector review – media 1/2

Structural and economic fluctuation-based drivers

The growth of the media sector is currently influenced by several different structural, legislative and economic fluctuation-based drivers.

The main driver of the media sector has been for a long time already the structural revolution arising from digitalisation and demographic factors, which shapes consumer and advertiser demand as well as the competitive field of the media industry and disrupts business models. The revolution is most evident in the sharp decline of the media profit trend as well as the increased demand for digital media.

The general economic trend (GDP change), which has historically had a strong correlation with the advertising income trends, specifically, has been left in the shade of structural change as a demand driver. However, short- and medium-term GDP changes will still have a significant effect on the revenues of media companies.

In addition, media companies are strongly affected by technological development, the partial blurring of the borders of the media sectors as well as legislative and cultural factors that shape the competitive dynamic between media companies and social media, in particular.

Key trends of the media sector

In our view, the key media sector market trends for investors are:

- The use of and demand for traditional media (newspapers, magazines, books and linear TV) will decrease, which will gradually reduce the content and advertising revenues of print media and undermine their profitability.
- The consumption of digital contents and media will increase and become more diverse, for example, due to the increasing popularity of mobile devices and applications. This increases digital content and advertising revenues and improves relative profitability.
- The competitive media field will become more globalised, and access to contents and data will become faster and easier, which especially weakens the competitive position of small media companies as well as media companies specialising in print media and increases competition for content revenues and investments in advertisement.
- The willingness to pay for digital contents will increase and the pricing models will develop, accelerating the growth of digital content revenues.
- Advertising will become automated and more effective, which will shape the structure and pricing of the digital ad market.
- The quantity and importance of data will increase, creating new business opportunities and services.
- Data protection and privacy requirements will increase. One of these drivers is the EU's General Data Protection Regulation (GDPR), which levels the playing field between local media companies and global platform operators.
- Technological know-how as a competitive factor will be emphasised.

Advertising market trends and prospects

In the last few years, the most influential trend on the Finnish advertising market has been the sharp decline of print media and, equally, the increase of digital advertising. The growth rate of the Finnish advertising market is clearly lagging behind the GDP trend, which explains the relatively large share of print media of the overall market, for example. In the last few years, the statistics describing advertising as a whole have become slightly less comprehensive, as a significant part of advertising investments has been directed at global operators excluded from the calculation, such as Facebook and Google. Advertisers have also invested heavily in the deployment of new advertising technologies, which has decreased direct investment in media advertising.

Judging by advertising channel, the growth of the advertising market has been very two-way. In Finland, advertising in magazines and newspapers has halved in the 2010s, and the amount of TV advertising has also dropped sharply. On the other hand, the amount of digital advertising has doubled in the 2010s, and its share of advertising as a whole (incl. Facebook and Google) has climbed to approx. 37%. In other words, it has overtaken newspaper advertising (approx. 20%), which has dropped to second.

Roughly half of the value of digital advertising constitutes advertisements on Facebook and Google. The other half comprises ads sold by national operators (such as Sanoma and Alma Media). The fastest-growing trends within digital marketing are social media marketing, mobile marketing and native advertising.

In the next few years, we expect the structural trends of the advertising market to continue largely as they are and the overall demand for advertising in Finland to become negative due to the decline of print media advertising. We also deem it possible that the regression caused by the coronavirus pandemic will accelerate the decline of print media, with advertisers reconsidering their investments in advertising.

Media sector drivers and trends

Digitalisation

New devices, new digital services and applications, faster network connections and the growing part of “digital natives” of the population have strongly digitalised media consumption.

Economic trend

Traditionally, the media sector has been very sensitive to economic fluctuations because over 50% of the revenues come from advertising. With digitalisation, the percentage of content revenue of the net sales is growing, which makes the sector less sensitive to economic fluctuations.

Technological development

New technologies will change the earning models and competition dynamic. Especially the role of data and analytics as a competitive factor will be highlighted. The main competitors are global platforms and technology companies.

Regulation and culture

Data protection and privacy regulation will become stricter, increasing the importance of fixed customer relationships. So-called ‘fake news’ will increase the role of well-known and trusted content providers.

Strong growth of digital media

- Internet- and mobile-based media consumption is growing
- Advertising becomes automated, its volume and effectiveness will increase and its price will drop
- Data quantity and value will increase
- Media consumption becomes fragmented and its availability will grow and become faster
- The use of digital contents will increase
- The importance of data protection and privacy will increase

Declining demand for printed and linear media

- Decreasing content and advertising revenues
- Weakening economies of scale and profitability
- Continuous need for improved effectiveness and consolidation

Sector review – media 2/2

According to TNS Kantar, the online advertising volume in Finland has grown in the last few years on average by 5–10% annually, and we estimate that the growth will continue at the same rate in the long run. We expect the linear TV advertising trend to maintain its slight decline (-5–0%) in the next few years, as some of the investments previously made in TV advertising will in our estimate be redirected to digital advertising and streaming services.

Content revenue trends

There are no reliable statistics pertaining to the market trends of content revenue. However, based on the content sales trends of Sanoma and Alma Media as well as the survey conducted by OKM, we estimate that content revenues as a whole decreased only slightly (-3–1%) in 2012–2019. In our estimate, the decline was sharpest in the sales of news-stand copies of tabloids and magazines.

The decrease of content revenue has been curbed by price increases and, especially, the accelerated growth of digital content sales. Even though the share of digital content sales overall remains relatively low, the largest media operators, such as Sanoma and Alma Media, have successfully managed to increase the number of subscribers paying for digital contents. For example, in the last few years, Sanoma has managed to increase the total number of Helsingin Sanomat subscribers for the first time in a long time, with the number of users paying for digital subscriptions rising to nearly 70% of the total number of subscribers – more than double the figure of 2012.

The growth in the number of digital content subscribers has been accelerated by the greater willingness to pay for digital contents, boosted by the increasing popularity of digital services, such as Netflix and Spotify, debate regarding fake news, the measures to develop paywalls and contents subject to a charge as well as the improved availability of digital services. The majority of digital service subscribers are under the age of 50. That said, the growth of digital content sales has strongly focused on the news and financial media; the digital subscription revenue trend of magazines has been muted.

The demand for print media content appears to continue its steady decline, and the average age of subscribers of printed newspapers has risen to approximately 60. It is our estimate that the printed newspaper subscription revenues will be halved within the next ten years. In addition to this, the lowering of the VAT rate for digital publications to the same level with the print media (10%) introduced in the summer of 2019 is likely to accelerate the switch from print to digital media.

We estimate that the growth of the total quantity of content revenue will hit zero in the next few years, as the growth of digital content revenues does not yet fully compensate for the decline in print media revenues.

Growth of digital contents improves relative profitability

One of the positive effects of the digital revolution of the media sector is that the growth of the relative share of digital revenues makes the sector relatively more profitable. The improved relative profitability is based on the sales margin of digital products and services, which is typically clearly higher than that of print media products as a result of lower distribution and material costs. The scalability of digital operations is also markedly better than that of the print media. According to our estimate, the EBIT % of media operations relying solely on digital content and advertising revenue is by approximation 20–30%, whereas the EBIT % of print media is typically within the 5–15% bracket.

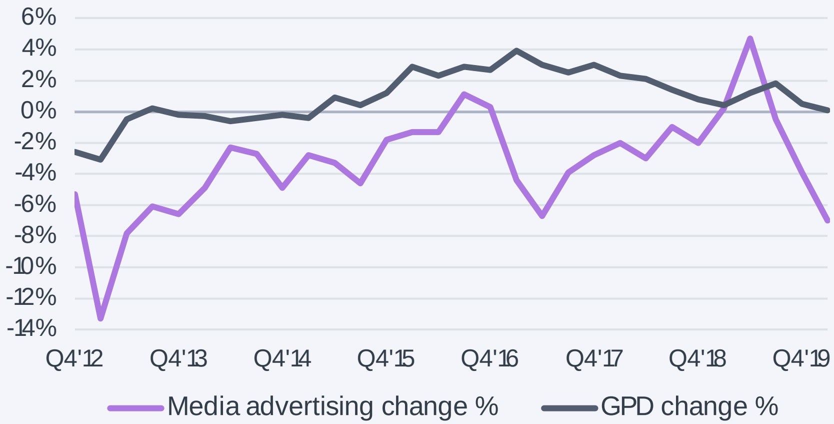
Global giants rule the competitive field

Digitalisation will continue to strongly shape the competitive media field, and competition in advertising will mainly take place against global platform companies, like Facebook or Google, instead of between local media companies. When it comes to content revenues, competition in print media and services is still local. However, when it comes to contents, TV and the digital media increasingly compete with global companies as well as companies outside the media industry (such as Apple or telecommunications operators).

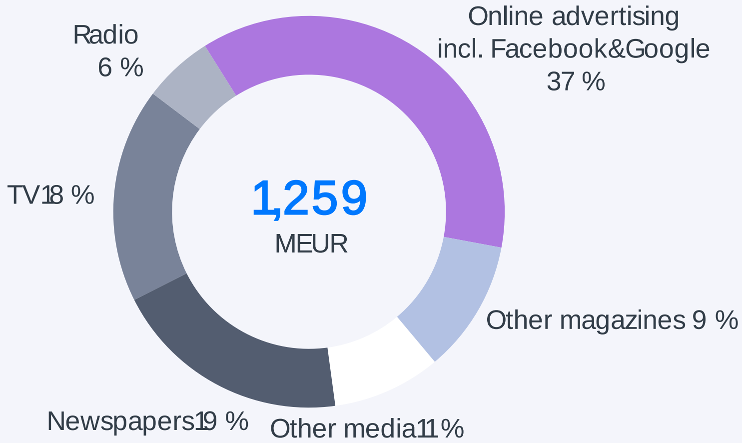
So far, the leading Finnish media companies have fared relatively well against the likes of Facebook and Google, and their share of the digital advertising and content market has remained high in a global comparison. In terms of content revenues, the Finnish media companies are helped by the high threshold to enter a small market and linguistic region, the readers' long and strong relationship with the print media as well as strong brands. Sanoma also clearly benefits from its multiple channels, which other Finnish or global platform or media companies cannot offer.

The development and competitive field of the media sector

The Finnish media advertising trend vs. GDP until Q1 2020

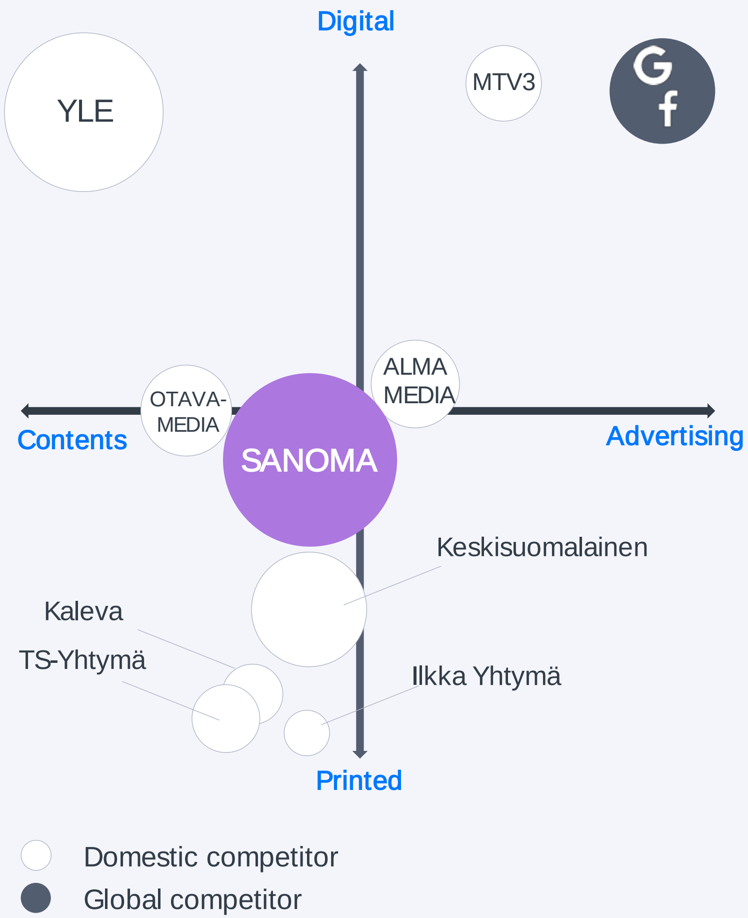


The Finnish media advertising distribution, 2019



Source: Kantar TNS, IAB, Statistics Finland, Inderes

The competitive field of the Finnish media market



The size of the sphere depicts the size of the Finnish media operations based on the financial statements and the assessments of Inderes. In terms of content revenues, YLE has been deemed a competitor of Sanoma, even though its operations are financed by public funds.

Media Finland 1/4

Sanoma's larger segment

Measured on net sales, Media Finland is Sanoma's larger segment (2019: MEUR 577/63% of Sanoma's net sales), but measured on the operational EBIT, it is the Group's smaller segment (2019: operational EBIT % 11.9%, operational EBIT MEUR 69 or 49% of Sanoma's adj. EBIT).

The segment's strategy is focused on three units: news & feature, entertainment and b2b marketing solutions. News and feature comprises the news media HS and Iltasanomat. Equally, entertainment covers the TV and radio company (Nelonen Media), the audio content service Supla as well as live events. The B2B marketing solutions include advertising sales as well as digital marketplaces. Part of the segment also comprises Sanoma Lifestyle, which is mainly focused on printed magazines (including Donald Duck, ET and Kodin Kuvalehti), as well as the independent business unit Oikotie.fi.

Media Finland is the largest commercial media company in Finland, measured by both the number of newspaper and magazine users and subscribers, printed & online media advertising as well as TV and radio advertising. Compared to the Finnish media advertising market calculated by Kantar TNS (approx. EUR 1.26 billion), Media Finland's market share is roughly 20% of the whole market and slightly below 20% of online advertising (approx. EUR 0.47 billion).

Revenues widely distributed – the print media weighting remains significant

Media Finland's business model is widely distributed to different revenue sources, the result of the segment's comprehensive product portfolio that covers the entire Finnish media sector. The impact of the media sector's structural trends on the segment's development continues to be significant because the share of print media revenues of Media Finland's net sales was approximately 47% in 2019 (2017: 51%), while the share of the non-print media constituted approx. 53% of it.

Advertising revenues remain – by a slight margin – Media Finland's greatest singe source of revenue despite the long downward trend of media advertising in Finland, constituting approximately 43% of the segment's net sales in 2019 (2018: 43%). When it comes to the segment's advertising revenues, in our estimate, the steadily developing TV and radio advertising constitutes nearly 50%, the growing online advertising constitutes nearly 30% and the sharply declining print media advertising makes up roughly 20%.

Content revenues' (subscription revenues) share of the segment's net sales was approximately 42% in 2019 (2018: 43%), which introduced stability to the net sales. Of this, recurring subscription revenue made up roughly 80% and single issue sales made up roughly 20%. According to our estimate, the content revenues of printed newspapers and magazines still make up roughly two thirds of the content revenue, while the subscription revenues of the digital subscriptions of the news media (HS.fi) and video services (Ruutu.fi) make up approximately one third of the content revenue.

Other business revenues comprised approximately 15% of the segment's net sales in 2019 (2018: 14%). We estimate that slightly over 60% of this comprised festival and event operations, roughly 20% comprised marketing services and the remaining approximately 20% mainly comprised book publishing and printing services.

Media Finland in brief, 2019

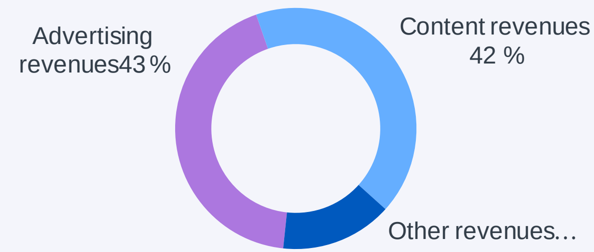
MEUR 577 (2018: MEUR 579)
net sales 2019

12.0% (2018: 12.0%)
Profitability, operational EBIT %

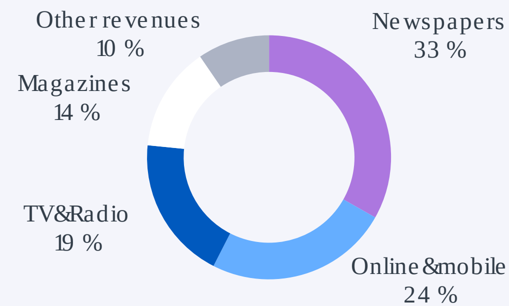
47%/53%
Share of printed/non-printed business revenues

#1st and #2nd market position
News media, magazines, TV&Radio, B2B

Net sales by revenue type, 2019



Net sales by product area, 2019



Source: Inderes, Sanoma

Media Finland 2/4

Segment's financial targets and strategy

Sanoma has set the following long-term financial targets for Media Finland: comparative net sales growth +/-2% & operational EBIT % excluding PPA depreciations 12–14%.

The long-term growth prospects of the news & feature entity are faint and two-way. This is reflected in the growth target of Media Finland as a whole, because almost 50% of the segment's revenues still rely on the print media market, which is going through strong decline caused by structural trends, and their share will increase further as a result of the regional newspaper operations acquired from Alma Media. Despite the structural decline of the print media, the company believes that the demand for digital contents will be sustainable and keep growing strongly. Subsequently, Media Finland's strategy is focused on a leading position in the news & feature segment. Therefore, the strategy is constructed around maintaining a leading position through the switch from print to digital, which also constituted the grounds for acquiring Alma Media's regional newspaper operations.

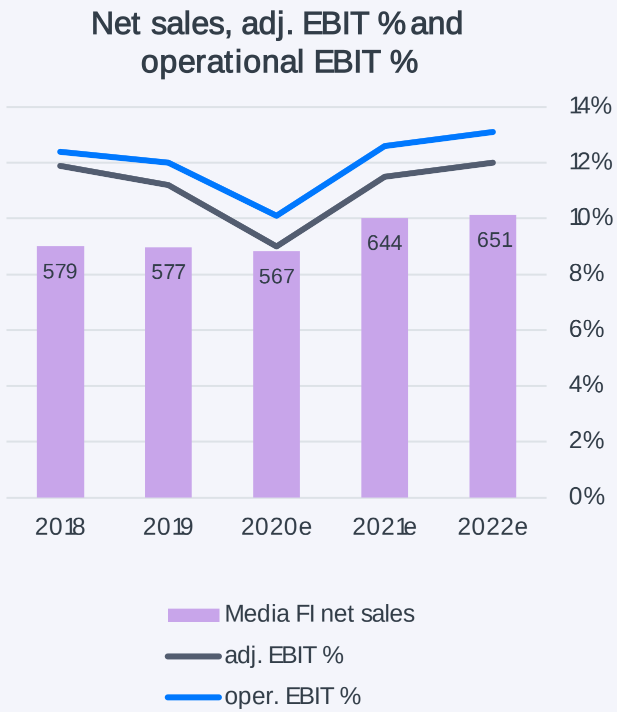
This said, due to the lower unit price of digital media, the switch from print to digital has a negative effect on the company's net sales. However, digital is much more scalable due to its cost structure and, consequently, more profitable. Regardless, speeding up the switch to digital is not strategically tempting because it is not be possible to quickly scale down the distribution and printing costs of print media, it would quickly decrease the advertising revenues, and all consumers are not ready to switch to digital consumption.

Financed by advertising, the TV & radio businesses, which generate 20% of the segment's revenues, have in our opinion faint growth prospects. However, this is compensated by the growth prospects of the digital services, which comprise nearly 25% of the segment's revenues. That said, a widespread presence on the different entertainment platforms is strategically sound because comprehensive availability brings significant value from the aspect of the advertising revenues arising from B2B advertising solutions. Reflecting this, up to 50% of the segment's advertising revenues come from entertainment. In our estimate, the medium-term growth prospects of the entertainment unit are good, which also supports the segment's stable overall growth target in the long term.

Media Finland's growth and profitability prospects

According to our estimate – and looking beyond the coronavirus pandemic – the segment's print media net sales will continue its 5% decline in the medium and long terms because the advertising revenues of the print media especially will continue to sharply fall, with the number of print media subscribers steadily decreasing. Considering Media Finland's current business structure, the media revenues other than the print media should grow altogether by approximately 3–5% per year, so the growth of the segment's total net sales over the course of the next couple of years should be slightly positive (approx. 1%), excluding M&A.

In our estimate, Media Finland can also be expected to continue its inorganic growth, so the realised growth will in all probability exceed the organic growth.



Media Finland 3/4

In terms of profitability, we also expect the segment to develop steadily in the medium and long terms. Profitability is negatively affected by the decline of the print media, investments in growth as well as cost inflation. According to our assessment, the company is still unable to fully compensate for these factors by means of more profitable (digital) services. That said, we still foresee that the company will gain benefits by improving the efficiency of its operations. However, their impact is clearly smaller than in the previous years.

Forecasts

The starting point of our forecasts is the assumption that the economic growth of Finland will sharply decline in 2020 as a result of the coronavirus pandemic and gradually recover in 2021–2022. We predict that Media Finland's net sales – boosted by the acquisition of Alma Media's regional newspaper operations – will remain relatively stable at approximately MEUR 567 in 2020 (-2% y/y). We project that, in 2021, the net sales to recover with the economy as well as the normalising festival operations and grow by 14% to MEUR 644.

We project that, in 2022, the net sales trend will be relatively stable. During the long-term projection period (2023–2026), we anticipate an approximate annual growth of 0–1%. Our net sales growth projections are in line with the segment's financial objective, excluding 2020 and 2021, which are exceptional due to the coronavirus pandemic.

We anticipate that Media Finland's 2020 operational EBIT will drop by approx. 17% to MEUR 57 (2019: MEUR 65) and the operational EBIT % to drop to 10.1% (2019: 12.0%). The reported EBIT will decrease slightly more (2020e MEUR 36 vs. 2019 MEUR 55) because, compared to 2019, the non-recurring items of 2020 are increased by the acquisition of Alma Media's regional newspaper operations. We have revised our projection regarding the non-recurring items of 2020 to MEUR -15 (prev. MEUR 8). We have also made slight adjustments to our projections, mainly reflecting the media advertising figures of April.

We anticipate that profitability will show strong signs of recovery in 2021 (operational EBIT growth of 42%), reflecting the recovery of the net sales as well as operational leverage and reaching a level corresponding to the financial targets. When it comes to 2022, we currently anticipate a slight increase in net sales and improving profitability. In the long term, we also project a slight increase in net sales and the gradual increase of the adjusted EBIT %, reflecting the increase of digital revenues. However, the increase of profitability is slowed down by the decline of relative profitability of the print media.

As a positive risk to our projections, we anticipate that media advertising will decrease less than expected in 2020 and/or correspondingly recover more in the wake of the coronavirus pandemic. Moreover, revenue growth-expediting acquisitions may speed up revenue growth faster than we anticipate. Apart from the short-term risks related to the coronavirus pandemic, negative uncertainty regarding the forecast is created especially by unpredictable long-term changes in the competitive position in digital advertising as well as the accelerated structural change of print media.

Media Finland projections

Profit and loss account	2018	2019	2020e	2021e	2022e
Net sales	579	577	567	644	651
Operational EBIT	72.0	69.2	57.3	81.3	85.3
Adj. EBIT	68.9	64.8	51.0	74.1	78.1
EBIT	61.7	54.9	36.4	71.1	75.1
Non-recurring items	-7.2	-9.9	-14.7	-3	-3

Growth and profitability	2018	2019	2020e	2021e	2022e
Net sales growth %	2%	-1%	-2%	14%	1%
Operational EBIT growth %	5%	-6%	-17%	42%	5%
Operational EBIT %	12.4%	12.0%	10.1%	12.6%	13.1%
Adj. EBIT %	11.9%	11.2%	9.0%	11.5%	12%
EBIT %	10.6%	9.5%	6.4%	11.0%	11.5%

Media Finland 4/4

Media Finland valuation

To a large extent, we determine the value of the Media Finland segment on the basis of the valuation coefficients of the peer group consisting of international media companies.

We have identified altogether 20 control companies for the Media Finland segment. Primarily, the peer group comprises combined print & digital media companies, similar to Sanoma, as well as a few TV companies. In our view, as a whole, the peer group's business models and growth prospects reflect Media Finland's business model as well as the sector's growth prospects reasonably well.

We have based the valuation on the peer group's 2021 EV/EBIT and EV/S coefficients as well as our projections regarding Media Finland's operational EBIT for 2021 (operational EBIT excluding PPA), as the peer group's 2020 projections entail a fair amount of uncertainty.

The peer group's average EV/EBIT and EV/S coefficients for 2021 that we have used are roughly at the 17x and 14x level, with the medians being 13.5x and 12x.

Using the peer group's medians for the 2021 valuation coefficients as well as Media Finland's net sales and operational EBIT projections, we have estimated Media Finland's corporate value (EV) at approx. MEUR 770–1,000, the average being MEUR 890.

Hence, Media Finland's value has remained relatively well aligned with the value we indicated in our previous comprehensive report (the 2019 estimate: MEUR 896). This has been especially affected by the fact that the revenue growth arising from inorganic growth is partly buried under the profit pressure caused by the coronavirus pandemic.

Oikotie's strategic assessment

Sanoma has set the Oikotie business unit under strategic assessment, which in our estimate means that the company is looking for a buyer for the unit. We expect that, were a suitable price on offer, the company would be willing to give the unit up because it is slightly disconnected from Media Finland's strategy. In our opinion, the unit would – due to its scale – be particularly valuable to a buyer with a foothold on synergic business operations. In 2019, Oikotie's net sales was MEUR 26 (2018: MEUR 24) and its operational operating profit was MEUR 10 (2018: MEUR 9), corresponding to an excellent operating profit margin of 38%.

According to our assessment, a growing and profitable digital business operation such as Oikotie can be priced using approximately 4–5 EV/S and 12–14 EV/EBITDA coefficients. Consequently, in our opinion, by selling Oikotie, the company would stand to make roughly MEUR 110–140, which would create leeway with regard to acquisitions in accordance with the company's strategy. A good control for the valuation is, for example, Autotrader NL, sold by Sanoma in 2016. Autotrader NL's net sales was approximately MEUR 6 in 2015, and Sanoma sold the company for roughly MEUR 28, corresponding to a 4.7x EV/S coefficient.

Media Finland's peer group

Control companies	EV	EV/EBIT		EV/S	
Company	MEUR	20e	21e	20e	21e
Alma Media	666	18.0	14.5	2.9	2.8
DMGT plc	1646	18.1	12.6	1.2	1.1
Future PLC	1347	16.4	13.0	3.8	2.8
Gannett	1485	19.4	10.4	0.5	0.5
GEDI	335	26.1	33.0	0.6	0.6
ITV PLC	4639	9.8	7.9	1.5	1.3
Lagardere	6431		21.8	1.2	1.0
Meredith Corp	3360	9.9	9.3	1.3	1.3
Arnoldo Mondadori Editore	469	13.0	9.2	0.6	0.6
Nordic Entertainment Group	2204	18.4	13.9	1.7	1.5
News Corp	6925	26.8	28.1	0.9	0.9
New York Times	5580	55.3	34.2	3.5	3.3
Promotora de Informaciones	1665	14.4	11.8	1.5	1.5
Prosiebensat 1 Media	5239	12.0		1.3	1.2
RCS	678	17.2	9.2	0.9	0.8
Roularta Media Group	75			0.3	0.3
Schibsted	6313	37.6	22.6	3.5	3.2
Axel Springer	7823	19.3	17.4	2.4	2.2
Tribune Publishing Co	345	7.8	7.0	0.5	0.5
TX Group	815	78.2	31.6	0.9	0.9
Average		**23.2**	**17.1**	**1.5**	**1.4**
Median		**18.0**	**13.5**	**1.3**	**1.2**

Financial situation

Financial situation strong and stable

Sanoma's financial situation has improved significantly in the last few years. All in all, it is now healthy and stable. The company has been able to turn its profitability around to a good level and compensate for the loss of print media revenues with digital revenues, the growth of Learning as well as M&A. Sanoma's balance sheet has reduced significantly due to the structural change, and the balance sheet's risks and leverage have fallen to a moderate level.

Sanoma's business model provides the company with a strong cash flow and, in practice, its organic growth ties up very little capital. Therefore, Sanoma's ability to pay dividends is good, and we expect Sanoma to continue increasing its dividends in the next few years. Thanks to its stronger balance sheet and financial position, the company is able to carry out important acquisitions (approx. MEUR 300).

The majority of the balance sheet entails intangible assets

The sum total of Sanoma's balance sheet at the end of Q4 2019 was MEUR 1,998 (Q4 2018: MEUR 1,519). The balance sheet has decreased significantly in just under ten years (2011: MEUR 4,328) as a result of M&A transactions, write-downs and sales of assets.

The balance sheet still comprises significant business value (MEUR 506, 25% of the balance sheet) as well as other intangible assets (MEUR 443, 22% of the balance sheet). The majority of the intangible assets are related to the business values of the magazine and learning business units as well as the activation of broadcasting rights and the costs of providing content. The company has a total of roughly MEUR 250 in intangible assets, shares and investments.

Due to the nature of the operations, the company's net working capital is clearly negative because the company accrues significant advance payments and tax-exempt liabilities are typically much higher than sales receivables. At the end of Q1 2019, the working capital was a negative MEUR 213 or approx. -23% of the net sales.

Sanoma's equity at the end of Q4 2019 was MEUR 529 or EUR 3.3 per share. Correspondingly, Sanoma had MEUR 629 in interest-bearing loans, MEUR 23 in liquid assets and MEUR 607 of net debt (incl. An IFRS 16 debt of MEUR 795).

In our view, Sanoma's balance sheet items are very saleable due to the significant restructuring and the company's strong turn of revenue. As a whole, the risks pertaining to the write-downs of the business value will be low in the near future.

Leverage to drop to a reasonable level

Sanoma's net gearing at the end of Q4 2019 was 139% (Q4 2017: 72%) and the ratio of net debt and the adjusted operating profit was at a high 2.7x level. It should be noted, however, that the sale of Media Netherlands and the acquisition of Alma's regional newspaper operations had a material effect on the figures, and we expect the net gearing at the end of 2020 to fall to a clearly lower 76% level and the ratio of net debt and the adjusted operating profit to drop to approximately 1.4x.

A healthy cash flow has supported dividend growth

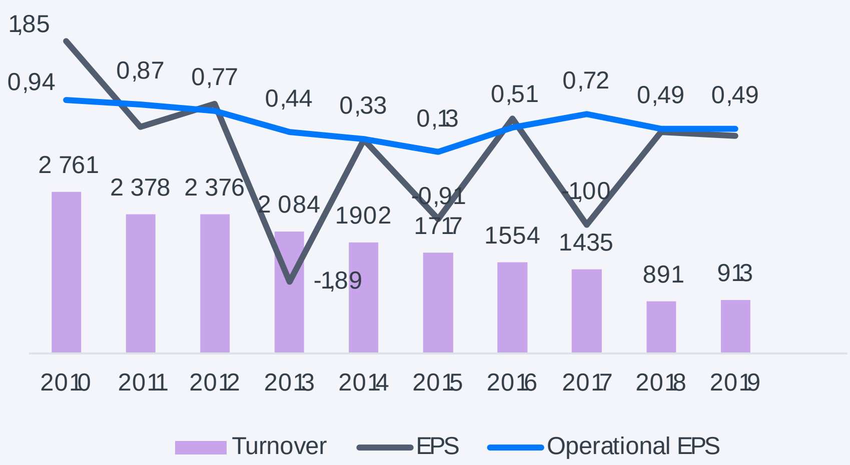
The cash flow of Sanoma's business operations was at a healthy approx. 10% level in 2017–2018 compared to the net sales, as it has improved dramatically with the improved profitability. In 2019, the operational cash flow rose up to 18%. However, the comparability is undermined by the effect of the IFRS16 standard, which moved rental liabilities to the financing cash flow (prev. operational cash flow). This had an approx. MEUR 25 effect on the operational cash flow. Taking into account the rental contract liability payments, the 2019 operational cash flow of MEUR 138 remained absolutely at the previous year's level (2018: MEUR 141). The company's capital expenditure in the last few years has been relatively stable; in 2019, it was MEUR 32. Therefore, the free cash flow per share (taking into account the part payment of rental contract liabilities) was EUR 0.65 per share (2018: EUR 0.67). The free cash flow reported by Sanoma, which does not take into account the part payment of rental contract liabilities, was respectively EUR 0.81 per share.

The company's dividend policy is to pay 40–60% of the free cash flow as dividends annually. The 2019 dividend was EUR 0.50 (2018: EUR 0.45 per share) and approximately 62% of the cash flow in accordance with the dividend policy. Compared to the EUR 0.65 free cash flow that takes into account the part payments of rental contract liabilities, the dividend corresponded to a nearly 77% dividend payment ratio.

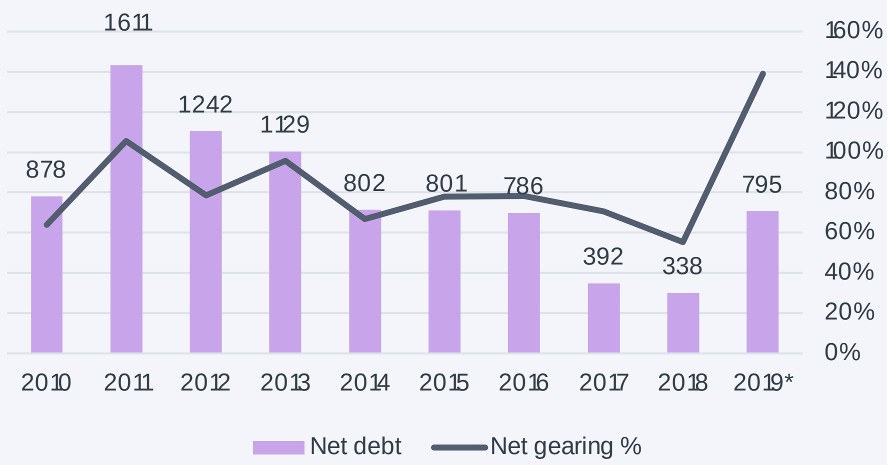
Therefore, the cash flow still enables the dividend to be increased in accordance with the dividend policy. However, the margin for increasing the dividend payment ratio is limited without using the balance sheet for support. This being the case, the condition for increasing the dividend per share in the long term is increasing the cash flow per share, not raising the dividend payment ratio.

Financial situation

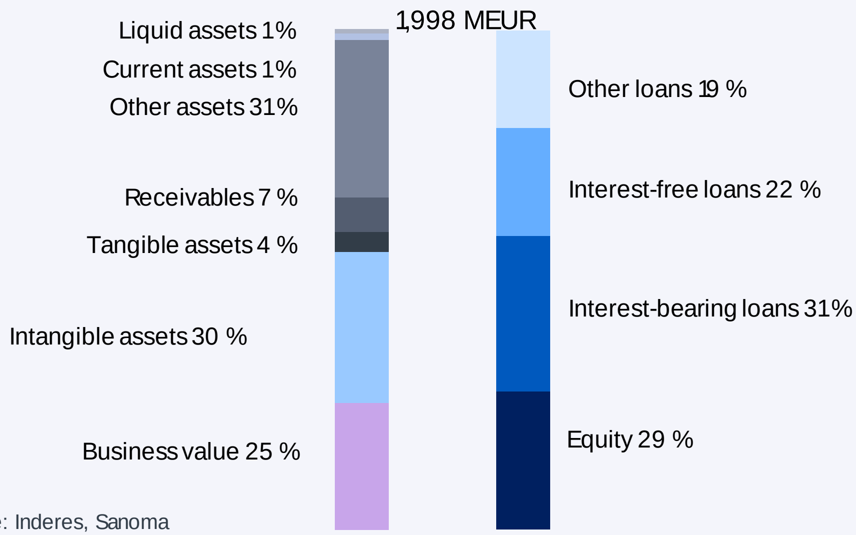
Net sales, EPS and operational EPS



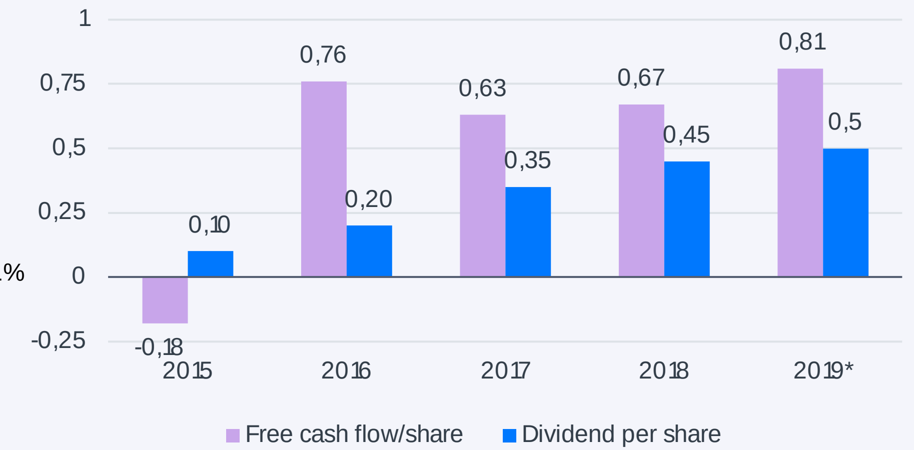
Net loans and net gearing %



Balance sheet structure, 2019



Free cash flow and dividend per share



Source: Inderes, Sanoma

* The IFRS-16 effect on net debt MEUR +188, on net gearing approx. +34% and on free cash flow approx. EUR 0.15/share

Forecasts at the Group level

2020: coronavirus puts pressure on Media Finland

Sanoma has relinquished the guidelines for the current year due to the coronavirus pandemic. Nevertheless, the company announced in late March that the decline in demand caused by the pandemic will have a material effect on Media Finland's advertising and event revenues from Q2 onwards; the net sales of events in 2020 is close to zero (2019: MEUR 35), and the company expects the annual advertising revenue trend to correspond to a financial crisis level (-17%). That said, the company does not expect the pandemic to affect Learning.

According to our projection, Sanoma's 2020 net sales will be MEUR 1,065. Consequently, based on the reported figures, we predict an approx. 17% increase in net sales. In our projection, almost all of the growth will result from M&A (incl. Iddink, Alma's regional newspapers), as we predict organic growth to be clearly negative as a result of the coronavirus. By segment, we expect Media Finland's net sales to decrease (-2%) and Learning's net sales go increase (+48%).

When it comes to the result, we anticipate that the adjusted EBIT excluding PPA depreciations will increase by approx. 14% to MEUR 154 (2019: MEUR 135) and the EBIT % excluding PPA depreciations will remain relatively stable at 14.3% (2019: 14.8%). In our forecast, the decline of the profit margin will be slowed down by Learning's improving financial performance, which compensates for the media business units' reduced profitability.

We predict that the adjusted result per share in 2020 will increase to EUR 0.62 (2019: EUR 0.49), reflecting the operational revenue growth and lower financing costs. Despite the increasing non-recurring items, we expect the reported result per share to increase to EUR 0.51 (2019: EUR 0.38). We anticipate that the free cash flow will show slight signs of decline. However, thanks to its strong balance sheet, the company will stick to its dividend policy and increase the dividend by 4%. We forecast that the dividend per share will rise to EUR 0.52 (2019: EUR 0.50).

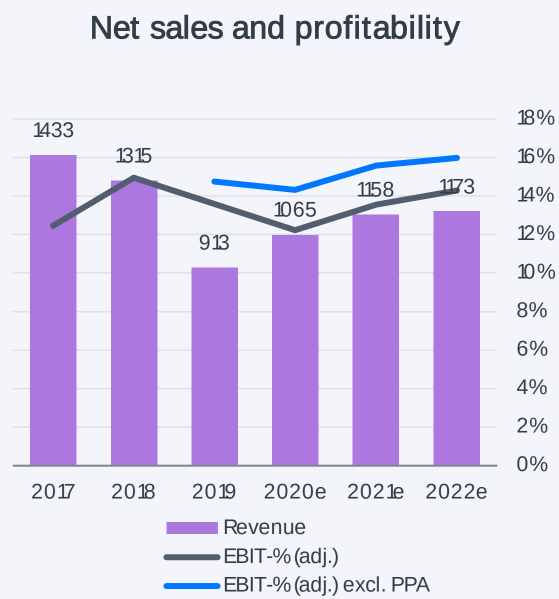
The 2021–2023 forecasts: Media Finland recovers, followed by steady revenue growth

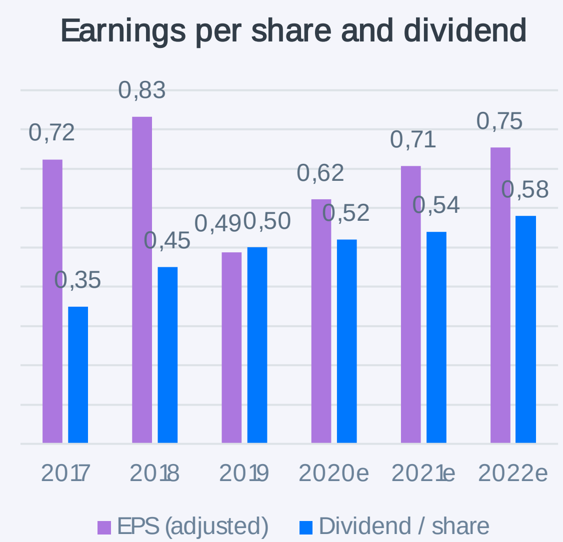
We predict that Sanoma's organic net sales will increase by 9% in 2021, with Media Finland recovering from the coronavirus-related dip and Learning continuing its steady growth. In 2022–2023, we expect the net sales trend to become stable, without new M&A. We project that profitability will increase clearly with the growing net sales in 2021 and increase lightly in 2022. Reflecting the moderate revenue growth, we expect a slight dividend growth in 2021–2022 brought by the moderate growth of free cash flow and the dividend payment ratio.

Long-term profit forecasts

The factors that inform Sanoma's financial performance in the long term are the growth rate of the scalable, highly profitable digital business as well as the steepness of print media's downward trend.

It is our projection that Sanoma's non-print media business operations will grow on average by 3–5% annually in accordance with the market growth but that the print media revenues, which make up approximately 30% of the revenues, will simultaneously drop by over 5% per year, bringing the overall growth of Sanoma's net sales to a lower level (2023–2028e 1%). That said, improved net sales distribution and efficiency as well as reduced depreciations increase Sanoma's EBIT margin (2028e: 15.5%) and revenue growth to a slightly positive level in our projection.





Forecasts at the Group level

Profit and loss account	2018	Q1'19	Q2'19	Q3'19	Q4'19	2019	Q1'20	Q2'20e	Q3'20e	Q4'20e	2020e	2021e	2022e	2023e
Net sales	1,315	163	260	285	206	913	188	272	382	223	1,065	1,158	1,173	1,186
Media Finland	579	132	155	147	144	577	130	137	142	157	567	644	651	653
Learning	313	31	106	138	61	337	58	135	240	66	499	514	523	533
Gross margin excl. non-recurring items		44	113	118	52	326	30	98	130	52	310	344	345	342
Gross margin	299	33	91	100	29	253	26	88	128	50	292	339	340	337
Depreciations	-131	-34	-38	-32	-47	-151	-44	-46	-43	-47	-180	-187	-177	-170
EBIT excl. non-recurring items and PPA	123	-6	61	73	-5	135	-8	58	93	10	152	180	187	189
EBIT excl. non-recurring items	197	-6	58	76	-3	124	-13	52	87	4	130	157	168	173
EBIT	168	-2	53	68	-18	102	-18	42	85	3	113	152	163	167
Media Finland	69	12	18	21	14	65	9	10	14	19	51	74	78	80
Learning	61	-18	42	56	-14	67	-20	45	75	-11	88	93	99	103
Other and eliminations	-10	-1	-2	-1	-3	-8	-2	-2	-2	-3	-9	-10	-10	-10
Net financing costs	-17	-5	-6	-7	-4	-22	-1	-2	-3	-3	-7	-12	-13	-13
Profit before tax	151	-7	47	61	-22	80	-18	41	83	0	105	141	151	155
Tax	-38	3	-13	-14	7	-17	5	-9	-18	0	-22	-31	-33	-34
Minority shares	-1	0	0	-2	0	-2	0	0	0	0	0	0	0	0
Net profit	111	-4	34	46	-15	61	-13	32	64	0	83	110	118	121
EPS (adjusted)	0.83	-0.06	0.24	0.32	-0.01	0.49	-0.05	0.26	0.41	0.01	0.62	0.71	0.75	0.78
EPS (reported)	0.68	-0.02	0.21	0.28	-0.09	0.38	-0.08	0.19	0.40	0.00	0.51	0.68	0.72	0.74

Key figures	2018	Q1'19	Q2'19	Q3'19	Q4'19	2019	Q1'20	Q2'20e	Q3'20e	Q4'20e	2020e	2021e	2022e	2023e
Net sales growth %	-8.2%	-37.7%	-28.4%	-27.5%	-31.0%	-30.6%	15.3%	4.9%	34.1%	8.5%	16.6%	8.7%	1.3%	1.1%
Adjusted EBIT growth %	10.1%	-178.0%	-26.9%	-17.1%	-118.8%	-36.9%	109.4%	-10.7%	15.3%	-234.5%	4.9%	20.7%	6.7%	2.9%
Adjusted gross margin %		27.3%	43.3%	41.3%	25.1%	35.7%	16.2%	35.8%	34.2%	23.2%	29.1%	29.7%	29.4%	28.9%
Gross margin %	22.7%	20.0%	34.9%	35.2%	14.2%	27.7%	14.0%	32.1%	33.6%	22.5%	27.5%	29.3%	29.0%	28.4%
Adj. EBIT % excl. PPA depreciations		-3.9%	23.4%	25.7%	-2.5%	14.8%	-4.4%	21.1%	24.3%	4.6%	14.3%	15.6%	16.0%	15.9%
Adjusted EBIT %	14.9%	-3.9%	22.4%	26.5%	-1.6%	13.6%	-7.1%	19.1%	22.8%	2.0%	12.2%	13.6%	14.3%	14.6%
Net profit %	8.5%	-2.3%	13.1%	16.1%	-7.1%	6.7%	-6.9%	11.6%	16.9%	0.2%	7.8%	9.5%	10.0%	10.2%

Source: Inderes

Investment profile

Sanoma will be profiled as a stable high dividend stock for investors

Sanoma's investor profile has changed significantly as a result of the structural changes in the last few years, and the company has changed from a relatively cyclical turnaround to a stable high dividend stock.

As part of this structural change, we estimate that the risk profile of the share has lowered, as the percentage of highly cyclical advertisement revenues of the net sales has clearly dropped and the company's business structure has become more streamlined. On the other hand, the company's cash flow profile and ability to distribute dividends have been improved by increased profitability, the significant reduction of debt and financing costs as well as reduced investments.

M&A in an important role

M&A is an important part of Sanoma's strategy. In addition, the developmental stage and trends of the sector increase the probability of M&A to high. In our estimate, the mergers and acquisitions will be visible to the investors in Sanoma in two ways: 1) Sanoma strives to actively accelerate growth by means of M&A; 2) Sanoma reshapes its business structure by selling the parts that do not fit its strategy. The size category of Sanoma's acquisitions varies a lot, but in all probability, even large acquisitions will not significantly alter Sanoma's operational risk profile. Potential acquisitions are not included in our forecasts before they are realised, as it is practically impossible to predict them.

In our opinion, Sanoma's key positive value-drivers for investors are:

Growth of digital operations: In our view, Sanoma's digital media operations have strong growth prospects and profitability, which is why they constitute a key value-driver for the share. In our estimate, the share of digital media operations (excl. linear TV & radio) of Sanoma's net sales is around 15%.

Gradual profitability improvements: The way we see it, Sanoma still has the potential to improve its profitability by streamlining its operations and improving its sales structure (e.g. Learning's growth) in the medium and long terms.

Strong cash flow: The ability of Sanoma's business units to produce cash flow is excellent. Over time, this enables both growing dividends, investments and paying off debt as well as significant acquisitions, if necessary.

Creating owner-value by M&A: Sanoma has a great potential to accelerate its revenue growth by means of M&A. According to our estimate, the main focus of M&A is on more stable Learning operations. Therefore, mergers and acquisitions provide the opportunity to change the net sales and profit structure towards more stable revenue components. The effect thereof would also reduce the risk profile.

In our opinion, Sanoma's key negative value-drivers and risks for investors are:

Reduced print media revenues: We expect the decline of Sanoma's print media net sales to continue far into the future, which will slow down the company's total growth and weaken its ability to produce a growing cash flow.

Weakening competitive position: The competitive field of media companies is fragmented, the sector-entry threshold is slower and competition for advertising investments has been increased by global operators (such as Facebook and Google). For these reasons, the competitive position of national, regional and local media companies has become weaker.

Technological risks: The key risks in the field of digital business operations are linked to technological changes that may rapidly change the markets and business models as well as significantly increase the costs of product development and advertising. At the moment, such risks include the increasing popularity of ad blockers as well as the strengthening position of social media tech platforms.

Risk of economic fluctuation: Although the sensitivity of Sanoma's operations to economic fluctuation has decreased markedly, weak economic fluctuations continue to lower the revenue growth expectations, especially for Media Finland, and it is also reflected in the sector's acceptable valuation coefficients. This is risk is highlighted especially in the short term with the sharp negative economic trend, specifically because there is a lot of uncertainty involved in the timetable of the revival of the economy.

M&A risks: Sanoma's history includes several failed mergers and acquisitions that have destroyed the value to owners. That said, the company has learned from its mistakes and the M&A risks are, in our view, lower than before.

Investment profile

1. Stable and profitable core operations that generate a strong cash flow

2. The chances of Group-level organic growth are weak due to the media's structural change

3. Moderate operational risk level: a strong market position, widely distributed revenues, low percentage of cyclical revenue

4. Improved profitability and balance sheet have created significant latitude regarding M&A

5. The expected share yield is strongly reliant on dividends as well as synergic acquisitions that accelerate revenue growth

Potential

- Digital revenue and service growth
- Better cost-effectiveness and net sales structure
- Improved cash flow and dividends
- Mergers & Acquisitions (M&A)

Risks

- Accelerated decline of print media, with the coronavirus pandemic severely slowing down the economic trend
- Weaker competitive position, especially compared to global competitors
- Failed M&A and integration
- Technological risks

Source: Inderes

Valuation 1/3

Valuation methods

When valuing Sanoma's share, we place a significant weight on the share's expected total yield based on the company's forecasts for the next few years (revenue growth + dividends + expected valuation coefficient change). In addition, we support valuation by means of the 'sum of parts' calculation, discounted cash flow (DCF) and valuation coefficient analysis. When it comes to valuation, we are especially in favour of the EV/EBIT coefficient because we think that it takes into account the differences between the financing structures of Sanoma and the control companies best.

Share's expected total yield

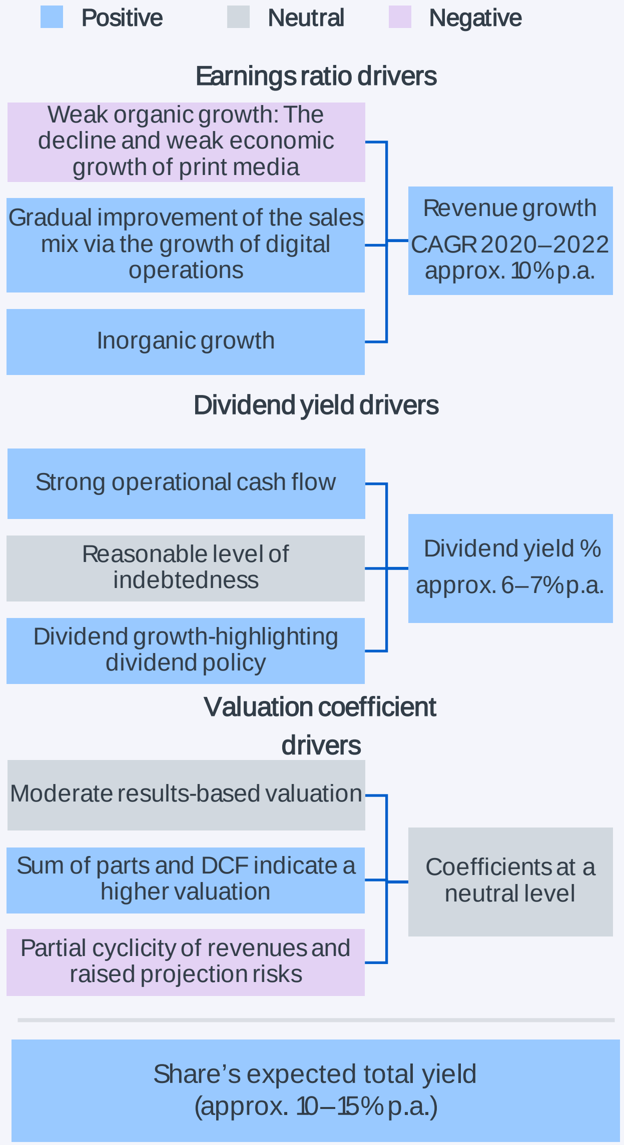
According to our estimate, Sanoma's share's expected yield will continue to strongly depend on the dividend yield in the next few years. However, the role of the revenue growth component has also clearly become more important. Calculated on the basis of our projections and the current EUR 8.6 price level, the share yield will be around 6–7% over the next few years. We estimate that the foundation of Sanoma's dividend is currently solid despite the volatility resulting from the coronavirus pandemic and the M&A transaction, as the company has a strong operational cash flow and balance sheet; the company has the potential to improve its cash flow in the next few years; and Sanoma's financial targets are strongly focused on dividend growth.

We expect Sanoma's adjusted net profit to grow to approx. 10% in the next few years, meeting the share's growth expectation despite the decreased visibility caused by the coronavirus. We also estimate that the company can be expected to make acquisitions in the next 12 months. However, we have not taken this into account in our projections because it is impossible for all practical purposes.

In our view, Sanoma's results-based valuation coefficients as a whole are neutral, both from an absolute and relative viewpoint, so the share's total expected yield remains at the healthy approximate 10–15% level.

The discounted cash flow (DCF), which describes the long-term potential as well as the independent valuation of the different business units, as well as the 'sum of parts' analysis indicate a clear growth potential for the share compared to the current level (approx. EUR 10–11). However, we do not anticipate Sanoma's share price to rise to this level within the next 12 months because, for us, the share's acceptable valuation includes some room for decrease due to the weaker outlook resulting from the print media's relative percentage as well as the coronavirus pandemic. Neither do we expect the separation of business units behind the 'sum of parts' analysis to become concrete over the short term.

Share yield drivers 2020–2022



Valuation 2/3

Sum of parts calculation

Sanoma's business units are highly independent, and there are no significant synergies between them. This is why, in our view, the 'sum of parts' calculation provides a solid yardstick for the valuation of Sanoma's share and adds transparency to the company's value creation. We have valued Sanoma's different business units separately in the previous chapters. Here, our focus is on the valuation of the whole entity.

Based on the basic assumptions and our projections, we estimate the gross value of Sanoma's parts at MEUR 2,092. From the aspect of its significantly improved earning power, Learning has, in our view, become Sanoma's most valuable part. We place its corporate value at MEUR 1,322. We have estimated the corporate value of Media Finland at MEUR 890.

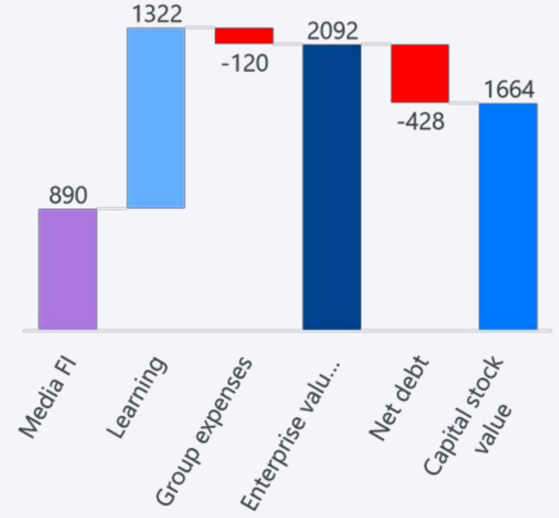
When the Group's fair value (MEUR -120) as well as its interest-bearing net debt at the end of 2020 (MEUR -428) are deducted from the segments' corporate values, the fair value of Sanoma's share capital based on the sum of parts is MEUR 1,664 or approximately EUR 10.2 per share.

Dismantling of the sum of parts is realistic in the medium term

We deem the dismantling of the value of the sum of Sanoma's parts realistic over the medium term because – as has already been stated – we think it probable that Sanoma's two mutually very different and non-synergic business units will eventually be separated into two independent companies.

In terms of increasing of the sum-of-parts value, it is essential to remember that, thanks to Learning's higher acceptable valuation coefficients, its revenue growth will be reflected more in the growth of the sum of parts. Indeed, we expect Sanoma to remain active in acquisitions, especially with regard to Learning. However, our current projections are based on organic growth and realised acquisitions.

Estimate of Sanoma's sum of parts, 5/2020



Distribution of the corporate value, 5/2020

Valuation 3/3

Discounted cash flow (DCF)

In our opinion, the discounted cash flow (DCF) model can be given a higher-than-average weight in Sanoma's valuation because Sanoma's financial situation has become established and the position of its business units is stable. Based on our DCF model, the share value is EUR 10.7. As a result of the decline of print media, the net sales will increase only slightly over the entire forecast period (2020–2028). However, thanks to the growth of the digital operations, Sanoma's relative profitability will gradually improve and its return on equity will remain at a healthy level. According to our model, the EBIT margin will rise from the 2020 level of 11.4% to 15.5% in the long term. In the model, the weight of the terminal period of the value of the cash flows is at a reasonable level of slightly below 50%. The weighted average cost of capital (WACC) we use in the cash flow model is 6.9%, with the cost of equity at 7.8%.

Weight analysis and control company valuation

According to our projections, Sanoma's 2020 adjusted P/E coefficient is 14x and the corresponding EV/EBIT coefficient is also 14x. As a whole, the coefficients are well in line with the medians of the previous four years and, based on the EV/EBIT coefficient, the share's valuation is also aligned with the historical, forward-looking EV/EBIT coefficient. Therefore, the absolute valuation coefficients indicate the share to be neutrally priced.

The average EV/EBIT coefficient of Sanoma's extensive group of control companies for 2020 is approximately 24x, with the median at the 18x level, indicating an approximate level of EUR 17.2–11.6 for Sanoma's share. However, Sanoma's revenue growth expectations are significantly more conservative than the peer group's average growth expectations, so we do not see a clear driver for value increase in this regard either. We also estimate that the coronavirus pandemic may undermine the reliability of the peer group's projections for the current year and have a negative effect on the peer group's absolute high valuation coefficients.

Valuation summary

Following Sanoma's recommendation to increase, we are increasing the target price of the share to EUR 9.5 (prev. EUR 9.0). In 2019–2020, Sanoma implemented significant M&A transactions, as a result of which the focus of the company's value creation has switched to the more defensive and highly profitable Learning business with stable growth prospects that is more attractive from the point of view of the investor profile. Although the media sector is struggling with the effects of the coronavirus in the short term, the media business will become more stable and profitable in the long term with the increasing digital subscription revenues. In our view, Sanoma will recover from the coronavirus-related shock with moderate losses, and the expected yield of the share is attractive considering the long-term potential, the normalised result and the strong dividend flow.

Sanoma's valuation coefficients

Valuation level	2020e	2021e	2022e
Share price	8.55	8.55	8.55
Number of shares, million	162.5	162.5	162.5
Market value	1389	1389	1389
Enterprise value (EV)	1860	1767	1696
P/E (adj.)	13.8	12.1	11.3
P/E	16.7	12.7	11.8
P/cash flow	3.3	7.5	8.4
P/B	2.6	2.4	2.3
P/S	1.3	1.2	1.2
EV/net sales	1.7	1.5	1.4
EV/EBITDA (adj.)	6.4	5.2	5.0
EV/EBIT (adj.)	14.3	11.2	10.1
Dividend/profit (%)	101.3%	79.9%	80.2%
Dividend yield %	6.1%	6.3%	6.8%

Source: Inderes

Sanoma's EV/EBIT coefficient trend

Source: Thomson Reuters

Peer group valuation

Peer group valuation	Share price	Market cap	EV	EV/EBIT		EV/EBITDA		EV/S		P/E		Dividend yield-%		P/B
Company		MEUR	MEUR	2020e	2021e	2020e	2021e	2020e	2021e	2020e	2021e	2020e	2021e	2020e
Media peers														
Alma Media	7,9	648	666	18,0	14,5	17,1	13,7	2,9	2,8	23,6	20,6	4,7	4,9	2,9
DMGT plc	720	1769	1646	18,1	12,6	13,5	11,1	1,2	1,1	32,5	22,2	3,3	3,4	2,1
Future PLC	1300,0	1397	1347	16,4	13,0	15,1	12,1	3,8	2,8	20,5	16,9	0,1	0,1	8,2
Gannett	1,4	178	1485	19,4	10,4			0,5	0,5		7,0	39,3	52,4	0,2
GEDI	0,5	234	335	26,1	33,0			0,6	0,6	80,0	76,7	1,1	1,1	0,5
ITV PLC	84,2	3662	4639	9,8	7,9	7,6	6,7	1,5	1,3	9,4	7,5	3,5	7,1	3,2
Lagardere	13,4	1727	6431		21,8	626,1	22,3	1,2	1,0		12,1	4,0	7,3	1,2
Meredith Corp	17,2	824	3360	9,9	9,3			1,3	1,3	3,9	4,0	13,3	13,3	
Arnoldo Mondadori Editore	1	264	469	13,0	9,2			0,6	0,6	14,9	9,0	2,7	4,0	1,4
Nordic Entertainment Group	280,0	1730	2204	18,4	13,9	16,4	13,6	1,7	1,5	19,6	14,0	2,2	2,7	7,7
News Corp	12,1	6504	6925	26,8	28,1			0,9	0,9	74,3	65,0	1,6	1,7	0,8
New York Times		5974	5580	55,3	34,2			3,5	3,3	76,3	52,4	0,3	0,3	
Promotora de Informaciones	0,6	410	1665	14,4	11,8			1,5	1,5	11,0	14,5			
Prosiebensat 1 Media	11,9	2791	5239	12,0		10,5	8,5	1,3	1,2	11,0	7,9	3,6	6,2	2,1
RCS	1	357	678	17,2	9,2			0,9	0,8	19,6	6,4		5,1	1,2
Roularta Media Group	13,0	170	75					0,3	0,3	20,6	25,5			
Schhibsted	240,2	5180	6313	37,6	22,6	35,0	20,0	3,5	3,2	68,2	35,3	0,7	0,9	4,3
Axel Springer	51,3	5515	7823	19,3	17,4			2,4	2,2	24,1	21,2	4,7	5,1	1,9
Tribune Publishing Co	10,0	336	345	7,8	7,0			0,5	0,5	13,4	11,4			
TX Group	66,3	692	815	78,2	31,6	10,7	9,9	0,9	0,9					0,4
Learning peers														
Bloomsbury Publishing PLC	220,00	195	175	9,9	17,1	9,9	18,2	0,9	1,1	13,4	25,2	2,2	3,8	
Houghton Mifflin Harcourt Co	1,84	228	727					0,6	0,6					0,9
Cengage Learning Holdings II Inc	12,75	819	2598											
Pearson PLC	460,70	3842	5194	13,4	11,1	11,6	10,2	1,3	1,2	12,7	11,1	4,1	4,4	0,8
Scholastic Corp	30,97	983	770		53,0			0,6	0,5		90,2			
K12 Inc	24,73	902	878	35,1	19,3			0,9	0,9	45,9	31,6			
John Wiley & Sons Inc	41,21	2089	2707	17,8	17,1			1,6	1,6	19,3	19,2	3,2	3,3	2,0
Wilmington PLC	130,50	123	182	15,1	8,2	15,2	8,3	1,5	1,4	16,5	8,0		7,0	
Koninklijke Brill NV	18,40	35	40											
2U Inc	36,36	2028	2125					3,3	2,8					4,1
Rosetta Stone Inc	18,38	426	395					2,3	2,1					
Chegg Inc	61,99	6826	6961	55,2	40,8	60,8	44,5	14,0	11,4	53,8	44,6			15,3
Sanoma (Inderes)	**8,55**	**1389**	**1860**	**14,3**	**11,2**	**6,4**	**5,2**	**1,7**	**1,5**	**13,8**	**12,1**	**6,1**	**6,3**	**2,6**
Average				**23,5**	**19,0**	**65,3**	**15,3**	**1,9**	**1,7**	**29,8**	**25,4**	**5,2**	**6,7**	**3,1**
Median				**17,9**	**14,5**	**15,1**	**12,1**	**1,3**	**1,2**	**19,6**	**18,1**	**3,2**	**4,2**	**2,0**

Source: Thomson Reuters/Inderes

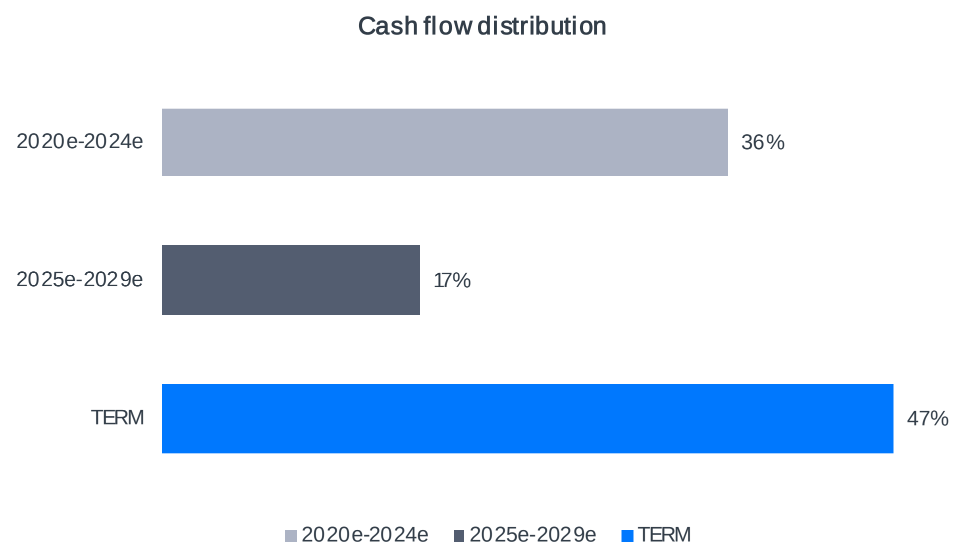
Discounted cash flow (DCF)

DCF model	2019	2020e	2021e	2022e	2023e	2024e	2025e	2026e	2027e	2028e	2029e	TERM
EBIT (operating profit)	**102**	**113**	**152**	**163**	**167**	**172**	**178**	**183**	**188**	**193**	**195**	
+ Depreciation	151	180	187	177	170	168	150	150	151	152	153	
- Paid taxes	22,1	-22	-31	-33	-34	-34	-36	-37	-38	-39	-40	
- Tax, financial expenses	-4,7	-1,5	-2,7	-2,8	-2,9	-3,6	-3,4	-3,3	-3,3	-3,2	-3,3	
+ Tax, financial income	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
- Change in working capital	-447,8	392	19,2	4,2	3,7	3,5	3,6	2,4	2,4	2,5	2,5	
Operating cash flow	**-177,6**	**661**	**325**	**309**	**304**	**306**	**293**	**296**	**300**	**305**	**308**	
+ Change in other long-term liabilities	-14,9	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
- Gross CAPEX	-109,7	-251	-141	-143	-145	-147	-150	-152	-154	-158	-170	
Free operating cash flow	**-302,2**	**410**	**184**	**166**	**159**	**158**	**144**	**144**	**146**	**147**	**138**	
+/- Other	134	13,1	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
FCFF	-168,0	423	184	166	159	158	144	144	146	147	138	2341
Discounted FCFF		**408**	**166**	**140**	**125**	**117**	**98,9**	**92,5**	**87,7**	**82,7**	**72,5**	**1233**
Sum of FCFF present value		2622	2214	2048	1909	1784	1667	1568	1476	1388	1305	1233

Enterprise value DCF	**2622**
- Interesting bearing debt	-780,6
+ Cash and cash equivalents	16,3
-Minorities	-55,6
-Dividend/capital return	-81,3
Equity value DCF	**1734**
Equity value DCF per share	**10,7**

Wacc	
Tax-% (WACC)	22,0 %
Target debt ratio (D/(D+E)	15,0 %
Cost of debt	3,0 %
Equity Beta	1,00
Market risk premium	4,75 %
Liquidity premium	0,00 %
Risk free interest rate	3,0 %
Cost of equity	**7,8 %**
Weighted average cost of capital (WACC)	**6,9 %**

Source: Inderes



Summary

Income statement	2017	2018	2019	2020e	2021e
Revenue	1433,4	1315,4	913,2	1065,1	1157,6
EBITDA	-48,1	299,2	252,8	292,5	339,2
EBIT	-239,0	168,4	102,0	112,6	152,1
PTP	-260,9	150,9	80,2	105,4	140,8
Net Income	-299,3	124,2	11,6	96,5	109,8
Extraordinary items	-417,6	-28,2	-22,1	-17,6	-5,0

Balance sheet	2017	2018	2019	2020e	2021e
Balance sheet total	1589,2	1519,0	1997,9	1470,2	1437,5
Equity capital	554,6	611,5	550,9	566,4	592,0
Goodwill	934,6	935,7	505,8	560,8	560,8
Net debt	391,8	337,9	764,3	428,2	336,9

Cash flow	2017	2018	2019	2020e	2021e
EBITDA	-48,1	299,2	252,8	292,5	339,2
Change in working capital	-45,7	-21,5	-447,8	392,2	19,2
Operating cash flow	-139,0	236,7	-177,6	661,5	324,9
CAPEX	749,9	-111,6	-109,7	-251,4	-140,6
Free cash flow	469,2	136,0	-168,0	423,2	184,3

Per share data	2017	2018	2019	2020e	2021e
EPS (reported)	-1,85	0,68	0,38	0,51	0,68
EPS (adj.)	0,72	0,83	0,49	0,62	0,71
OCF / share	-0,85	1,46	-1,09	4,07	2,00
FCF / share	2,87	0,84	-1,03	2,60	1,13
Book value / share	3,39	3,73	3,26	3,35	3,51
Dividend / share	0,35	0,45	0,50	0,52	0,54

Growth and profitability	2017	2018	2019	2020e	2021e
Revenue growth-%	-13 %	-8 %	-31%	17 %	9 %
EBITDA growth-%	-110 %	-722 %	-15 %	16 %	16 %
EBIT (adj.) growth-%	6 %	10 %	-37 %	5 %	21 %
EPS (adj.) growth-%	42 %	15 %	-42 %	28 %	14 %
EBITDA-%	-3,4 %	22,7 %	27,7 %	27,5 %	29,3 %
EBIT (adj.)-%	12,5 %	14,9 %	13,6 %	12,2 %	13,6 %
EBIT-%	-16,7 %	12,8 %	11,2 %	10,6 %	13,1 %
ROE-%	-47,6 %	19,2 %	10,8 %	15,5 %	19,7 %
ROI-%	-17,1%	17,2 %	8,7 %	9,4 %	15,4 %
Equity ratio	38,5 %	44,5 %	29,6 %	42,6 %	45,6 %
Gearing	70,6 %	55,3 %	138,7 %	75,6 %	56,9 %

Largest shareholders	% of shares
Jane ja Aatos Erkon Säätiö	24,4 %
Herlin Antti	11,9 %
Langenskiöld Lars Robin Eljas	7,5 %
Seppälä Rafaela Violet Maria	6,3 %
Helsingin Sanomain Säätiö	3,5 %
Keskinäinen Eläkevakuutusyhtiö Ilmarinen	2,2 %

Source: Inderes

Valuation multiples	2017	2018	2019	2020e	2021e
EV/S	1,5	1,3	2,6	1,7	1,5
EV/EBITDA (adj.)	7,2	5,8	9,3	6,4	5,2
EV/EBIT (adj.)	12,0	8,8	18,9	14,3	11,2
P/E (adj.)	15,0	10,2	19,4	13,8	12,1
P/B	3,2	2,3	2,9	2,6	2,4
Dividend-%	3,2 %	5,3 %	5,3 %	6,1 %	6,3 %

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Recommendation	Upside potential*
Buy	> 15 %
Accumulate	5 - 15 %
Reduce	-5 - 5 %
Sell	< -5 %

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Recommendation history (>12 months)

Date	Recommendation	Objective	Share price
26 April 2017	Reduce	€ 8.40	€ 8.09
25 July 2017	Increase	€ 8.40	€ 7.66
7 September 2017	Increase	€ 9.00	€ 8.43
26 October 2017	Increase	€ 10.20	€ 9.69
12 February 2018	Increase	€ 10.20	€ 9.95
15 March 2018	Increase	€ 11.00	€ 10.09
30 April 2018	Buy	€ 10.80	€ 9.00
25 July 2018	Increase	€ 10.70	€ 9.62
17 September 2018	Increase	€ 10.00	€ 8.71
12 October 2018	Increase	€ 9.50	€ 8.26
24 October 2018	Increase	€ 9.50	€ 9.05
13 December 2018	Increase	€ 9.50	€ 8.94
7 February 2019	Reduce	€ 9.50	€ 9.06
2 May 2019	Reduce	€ 9.00	€ 9.09
12 May 2019	Reduce	€ 9.00	€ 8.56
26 July 2019	Increase	€ 9.40	€ 8.90
16 September 2019	Increase	€ 10.00	€ 9.52
28 October 2019	Increase	€ 10.70	€ 10.16
12 December 2019	Reduce	€ 10.00	€ 9.47
18 December 2019	Increase	€ 10.00	€ 9.30
10 February 2020	Increase	€ 11.25	€ 10.64
12 February 2020	Reduce	€ 11.60	€ 11.62
25 March 2020	Increase	€ 8.50	€ 7.66
30 April 2020	Increase	€ 9.00	€ 8.51
29 May 2020	Increase	€ 9.50	€ 8.55

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