KH Group

Company report

8/15/2023

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Inderes corporate customer

This report is a summary translation of the report “Luvassa odotettu raportoinnin muutos H1:llä” published on 08/15/2023 at 8:30 am EEST.

Expected change in reporting in H1

KH Group's H1 report will be published on Thursday at 8 am. We have made some adjustments to the sum of the parts ahead of the report, but overall the SOTP remained close to our previous estimate. We still see clear value in the share relative to the low current share price and expect the value to gradually be released as the new strategy progresses. We reiterate our target price of EUR 1.20 and Buy recommendation.

Our estimates for Indoor 2023 were lowered and so was our view on the value of the holding

We lowered our estimates for Indoor from 2023, as market data from Statistics Finland for the furniture and furnishings sector shows a quarterly decline of around 8%, and the budding recovery we expected has not yet materialized. This is despite of normal spring weather this year, which is important for the sale of garden furniture, while last year there were a lot of unsold furniture. The fact that the Asko and Sotka stores in Iisalmi are being closed is also a sign of the weak development of the market. We now expect Indoor's Q2 sales to decline by 7% to EUR 43.4 million, but we still expect EBITDA (IFRS) to recover slightly year-on-year to EUR 4.7 million (Q2'22: 3.6 MEUR). The savings of around EUR 1 million/year from the change negotiations support the result slightly, as do the lower freight prices. The number of additional ERP entries should also be lower than in the comparison period. With our lowered estimates, we cut our estimate of the value of the Indoor holding to EUR 24.6 million (was 29.0 MEUR). The current year looks set to remain low for Indoor, but the ERP project should be completed in Q4 and its improved functionality, ERP implementation costs disappearing, and slowly recovering purchasing power should bring cash flow back to more normal levels in our 2024 estimate. Indoor's 2023e P/E ratio is very high as earnings are lagging, but the 2024e P/E ratio is only 8x once the market starts to normalize.

Another strong quarter expected for KH-Koneet Group, but slowdown in construction brings uncertainties

Our estimate for the KH-Koneet Group is unchanged and we expect its Q2 net sales to be at the level of the comparison period at EUR 54.7 million, but the EBITDA margin to decrease slightly to EUR 4.3 million (Q2'22: 4.5 MEUR). We expect that the slowdown in the construction market will start to counterbalance the good performance, so 2023 earnings will be slightly below 2022 levels. KH-Koneet Group's value of EUR 50.9 million is unchanged, and its 2023 P/E ratio remains at around 9x. In terms of value development of the target companies, the greatest potential is still directed at KH-Koneet, which, if strong growth continues, could increase its value clearly. For HTJ, we expect net sales growth and an improved EBITDA margin. Nordic Rescue Group's sales are depressed by Vema's exit from the figures, but EBITDA should turn positive when Vema no longer makes a loss for the company.

We still see hidden value in the parts

Overall, our sum-of-the-parts calculation remained close to our previous estimate, as the value of the Indoor holding declined and the selling price of Logistikas exceeded our expectations by EUR 1.5 million. We would also cut tax liabilities (-3.5 MEUR) from the SOTP, as we estimate that they will not be realized since the balance sheet value increase comes from KH-Koneet Group, which won't be divested. In our view, the market will start to look at the stock on an earnings basis in the future as reporting changes, whereas in the past the company's balance sheet-based pricing has played a key role. Our estimated earnings-based SOTP now stands at EUR 71.5 million, or EUR 1.23 per share, and relative to this, we believe the stock remains undervalued.

Recommendation

Buy

(previous Accumulate)

EUR 1.20

(previous EUR 1.20)

Share price:

1.01

	2022	2023e	2024e	2025e
EBIT adj.	-10.1	7.7	12.0	13.2
Net Income	-8.2	6.0	8.7	9.6
EPS (adj.)	-0.14	0.10	0.15	0.17

P/E (adj.)	neg.	9.7	6.7	6.1
P/B	0.8	0.6	0.6	0.5
Dividend yield-%	0.0 %	0.0 %	0.0 %	0.0 %
EV/EBIT (adj.)	neg.	9.8	6.4	5.9
EV/EBITDA	neg.	9.8	6.4	5.9

Source: Inderes

Our expectations for Thursday's H1 result

Revenue	H1'22	H1'23	H1'23e	Kasvu
MEUR	EBIT	Comparison	Inderes	Ennuste
Indoor Group	93		87	-6%
KH-Koneet Group	97		98	1%
Nordic Rescue Group	23		20	-12%
HTJ	10.5		12.9	23%

EBITDA	H1'22	H1'23	H1'23e	Kasvu
MEUR	EBIT	Comparison	Inderes	Ennuste
Indoor Group (IFRS)	6.8		9.0	33%
KH-Koneet Group	6.2		6.6	6%
Nordic Rescue Group	-0.3		0.7	-333%
HTJ	1.2		1.2	0%

Price below the conservative sum of the parts

Sum of the parts creates the basis for valuation

Company-specific estimates and the valuation multiples we use are presented in full on pages 5-8. Page 9 presents the valuation of the holdings' peer groups. The sum of the parts we calculate for the company is now EUR 71.5 million or EUR 1.23 per share. The company's ROE fell to -9.5% for the past 12 months. The company's strong track record in previous years has started to show signs of cracking. Indoor's operating environment has naturally been difficult and in the longer-term ROE % is still excellent.

Key future value drivers:

1) success in the development of KH-Koneet, 2) success in developing other target companies prior to exit so that sales prices can rise. We feel it was the right solution to focus on KH-Koneet, because we believe the greatest potential of the holdings lies here. As the strong growth of KH continues, it could increase its value clearly, both through earnings growth and an increasing acceptable valuation level. However, the cooling of the target market also brings short-term risks to earnings development.

Indoor's value for the company has in recent years come from its stable strong cash flow. Before the pandemic years (2013-2019), the Finnish furniture market was relatively stable and we believe that it will start stabilizing again from H2'23, when consumers' purchasing power starts to catch up to inflation. As the operating environment normalizes, the company will, according to our estimates, again grind out a strong dividend yield to its owners from 2024, since almost the entire net result can be paid out as dividends as working capital or investments only tie up limited amounts of capital.

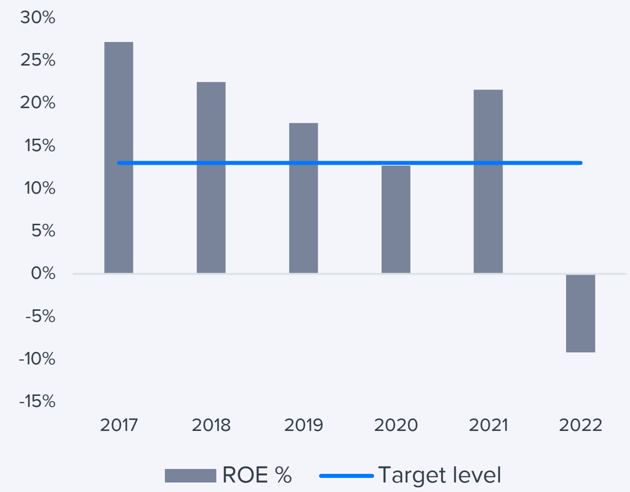
HTJ also generates good cash flow thanks to its capital-light business. At the current level of earnings, its value is already well placed to develop positively as net debt is reduced. The performance potential of NRG has clearly fallen after Vema Lift's bankruptcy. At the same time, the risks related to its turnaround have disappeared. The weight of NRG in our sum of the parts is very low.

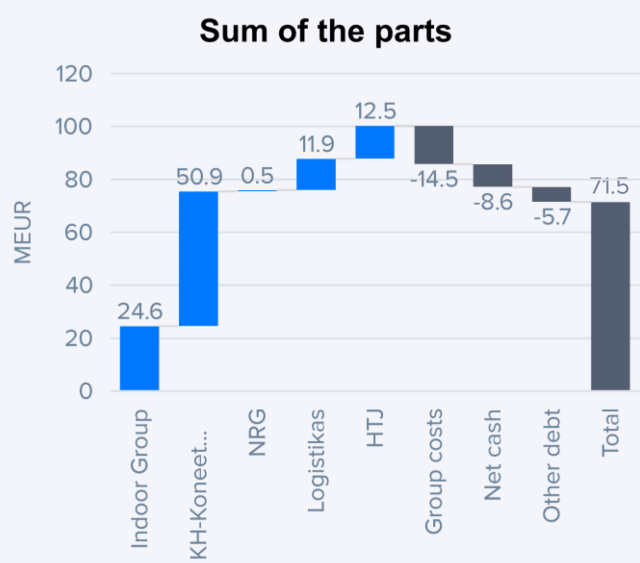
New strategy aims to release the value hidden in the parts

KH Group will first transform its operations from a private equity investment company into a conglomerate in H1'23. The root cause of the transformation into a conglomerate is that the earnings of the company's various unlisted holdings and group expenses are combined in the same income statement, balance sheet and cash flow statement (cf. e.g. Aspo). This makes it easier for investors to make their own assessment of the corporate cluster's value compared to the current model, where changes in the fair value of holdings in the balance sheet determine the company's result. We believe the change in reporting alone will move the share slowly toward the value indicated by our SOTP (now EUR 1.20).

Ultimately, KH Group intends to become an industrial group built around KH-Koneet Group and dispose of other target companies. On page 10, we have added our DCF calculation for KH-Koneet. The calculation indicates that KH-Koneet could independently be as valuable as KH Group's market cap at present and that the investor would thus in a way receive the other parts free of charge. The calculation is preliminary, as it is based on FAS accounting and the transition to IFRS accounting may result in substantial changes.

However, relying on the DCF model of KH-Koneet in valuation requires that the company proves the sustainability of its current strong performance also in a weaker market.





NB: The 'other liabilities' row in the sum of the parts relates to the redemption option of KH-Koneet's and HTJ's minorities

Indoor Group

Indoor Group generates strong cash flow in a normal market.

EV/EBITDA*	Estimated EV*	Holding	Holding
5.0x	119	58.3%	24.6
2023e	MEUR	2021	MEUR

Company description

Indoor Group Oy owns retail chains Asko and Sotka, and the company also includes the sofa factory Insofa Oy located in Lahti, as well as Indoor Group AS that is responsible for Estonian operations.

Investment story

Sievi Capital (current KH Group) acquired a majority holding in Indoor in 2017 from Kesko. During COVID years the company's performance was strong. The strategy updated in summer 2020 aims to continue improving profitability so that the EBIT margin would double from the 2019 level.

Business model

Indoor Group has a nationwide retail network in Finland. The importance of e-commerce has also increased in the company's multi-channel business model.

Competitive advantage

Indoor Group's competitive edge is well-known brands, good market position and the high volumes it generates. The own sofa factory in Lahti also enables demand-driven product tailoring for Asko.

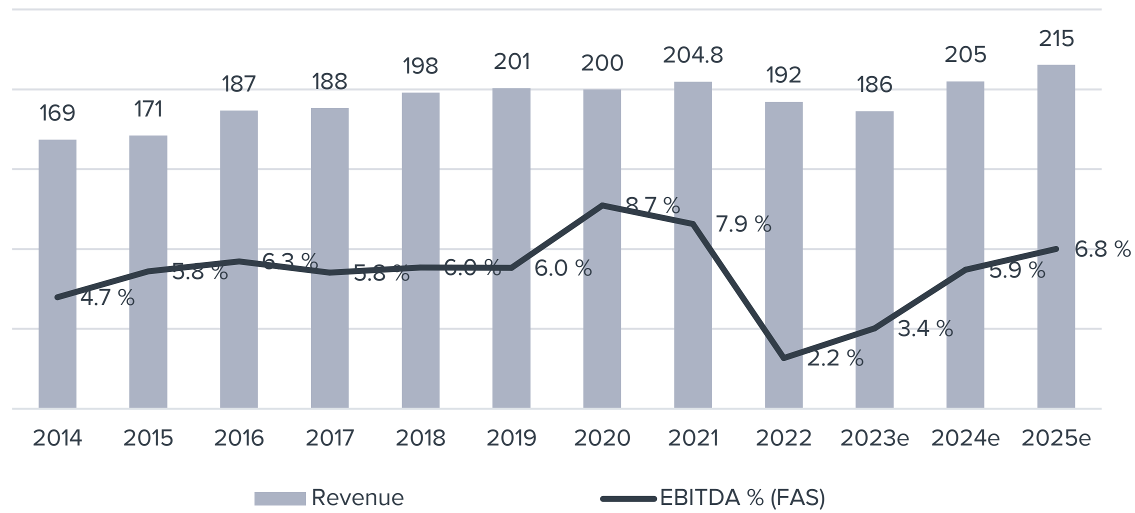
Estimate of earnings growth rate

Value creation potential

Risk profile

Source: Inderes

Key figures and estimates **(FAS):



Value drivers

- Sharpening brands and pricing
- Utilizing customer data
- The source of growth is expansion of product groups and e-commerce
- Strong cash flow and good return on capital
- Streamlining operations by harmonizing background processes

Risk factors

- Low consumer confidence and declining purchasing power lasting longer than expected
- Overall market growth has been slow before COVID
- Forcing growth through expensive acquisitions
- Tighter competition
- Successful upgrade of ERP system

Valuation

- Valuation with EV/EITDA ratios on level with the peer group when the non-recurring ERP system costs are adjusted. 2023 P/E ratios are, however, elevated as poor performance is particularly evident in the bottom line.
- We expect Indoor to return to generating a more normal result in 2024 when the P/E ratio is 8x.

*EV and EBITDA according to IFRS accounting **FAS accordant EBITDA in the graph to maintain a comparable time series In IFRS accounting, EBITDA is some EUR 17 million higher and net liabilities EUR 67 million higher than in FAS. The dip in profitability we expect in 2022 is also explained by the ERP project and the related cloud service investment (-3.2 MEUR) that is processed as a cost. We also expect another EUR 1 million in these costs in 2023. These costs have not been adjusted in the graph.

KH-Koneet Group

KH-Koneet Group has been a very successful investment as the company group has developed excellently since its formation.

EV/EBITDA	Estimated EV	Holding*	Holding
6.5x	79.7	100%	50.9
2023e	MEUR	2022	MEUR

Company description

KH-Koneet Group is an importer and retailer of construction and earth-moving machinery. It also offers maintenance and spare part services. The company also has an earth-moving machinery rental company founded in 2018 and in 2019 the company expanded to Sweden with an acquisition.

Investment story

Sievi Capital (current KH Group) invested in KH-Koneet Group in 2017. The growth of the group consisting of separate companies has been strong during the investment period. Now the company seeks profitable growth, especially in Sweden, where market shares are still low

Business model

KH-Koneet has a comprehensive network and service offering in Finland and now also in Sweden. There are very few intermediate stages in the supply chain. In the company's business model, the sellers are essential, and the cost structure is flexible with its success.

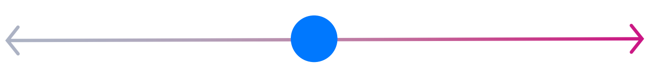
Competitive advantage

The company has also been able to build strong relationships and a good negotiating position to both manufacturers and customers. The company's agile and self-directed organization also brings a clear competitive advantage.

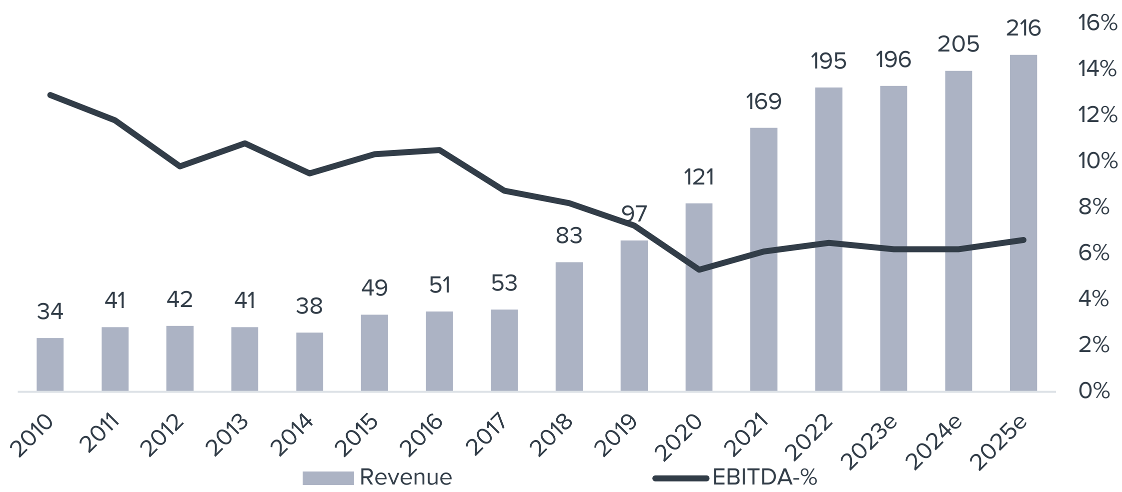
Estimate of earnings growth rate

Value creation potential

Risk profile



Key figures and estimates:



Value drivers

- Sales growth in Sweden through expansion of the network and representation
- Introducing the operating model of KH-Koneet to Sweden and raising profitability to the level of Finland
- Increase rental activities

Risk factors

- Success of the acquisition
- Deterioration of the market situation
- Tightening competition
- Manufacturer's M&A transactions
- Effect of component shortage on availability
- As the Group grows, maintaining a self-directed culture can create challenges

Valuation

- We currently value the company with a conservative EV/EBITDA ratio of 6.5x with 2023 estimates
- A discount to peers is justified as the peers are large companies that manufacture construction and earth-moving machinery and that are priced at a premium compared to importers.

2010-2016 figures are pro-forma figures including Edeco Tools Oy, KH-Koneet Oy, KH-Engineering Oy

*The company's holding at the end of 2022 was 90.7%, but it has an option to increase its holding to 100%

Source: Inderes

Nordic Rescue Group

The acquisition was completed in February 2020 and has so far been a clear failure for the investment company.

EV/EBITDA	Estimated EV	Holding	Holding
6.0x	11.4	68.1%	0.5
2023e	MEUR	2022	MEUR

Company description

Saurus' premises are located in Jyväskylä and Sala Brand's in Sweden. The Group has a strong position on its domestic markets in Finland and Sweden.

Investment story

The former owner of the companies Kiitokori sold the companies in a generation changeover. Under the company, NRG's story has been bumpy, as Vema Lift failed to deliver on its promises concerning international growth. Vema Lift was declared bankrupt at the end of 2022.

Business model

Saurus' and Sala Brand's business consists of the assembly of rescue vehicles. Sales is targeted directly at domestic end customers.

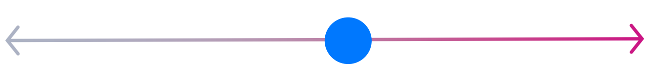
Competitive advantage

Strong brands and market position in Finland and Sweden, skilled personnel and long customer relationships also bring competitive advantages.

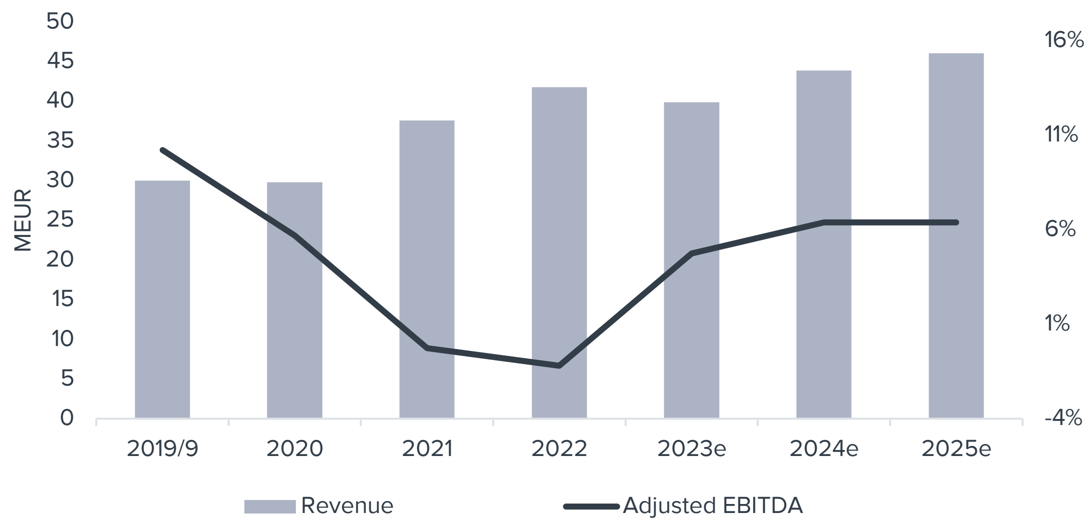
Estimate of earnings growth rate

Value creation potential

Risk profile



Key figures and estimates:



Value drivers

- After Vema Lift's bankruptcy, the focus is on the Finnish and Swedish markets
- Easing of component shortage
- Increasing production capacity at the rate of demand
- Accelerating production lead times and improving working capital
- Adjusting the cost level of the parent company to the shrinking group

Risk factors

- Weakening economic situation
- Tightening competitive situation
- A new component shortage could again have a negative impact on platform deliveries, as the position in the value chain is not particularly good

Valuation

- Very limited impact on the value of the company due to the company's high debt burden

Source: Inderes

Rakennuttajatoimisto HTJ

Rakennuttajatoimisto HTJ is the company's latest acquisition carried out in October 2021.

EV/EBITDA 6.5x 2023e | **Estimated EV** 20.8 MEUR | **Holding*** 100% 2022 | **Holding** 12.5 MEUR

Company description

HTJ is a construction consulting company established in 1999. The company provides building construction management and supervision services, as well as building engineering services and infrastructure construction services.

Investment story

The market for the services provided by HTJ is estimated to have grown by an average of some 6% p.a. in 2015-2020. Under the company, HTJ also carried out its first acquisition (Infrap Oy spring 2022). In the past, the company has grown only organically.

Business model

The company focuses on expert activities that generate good ROE and cash flow. The foundation of the service offering is versatile construction management, supervision and project management services.

Competitive advantage

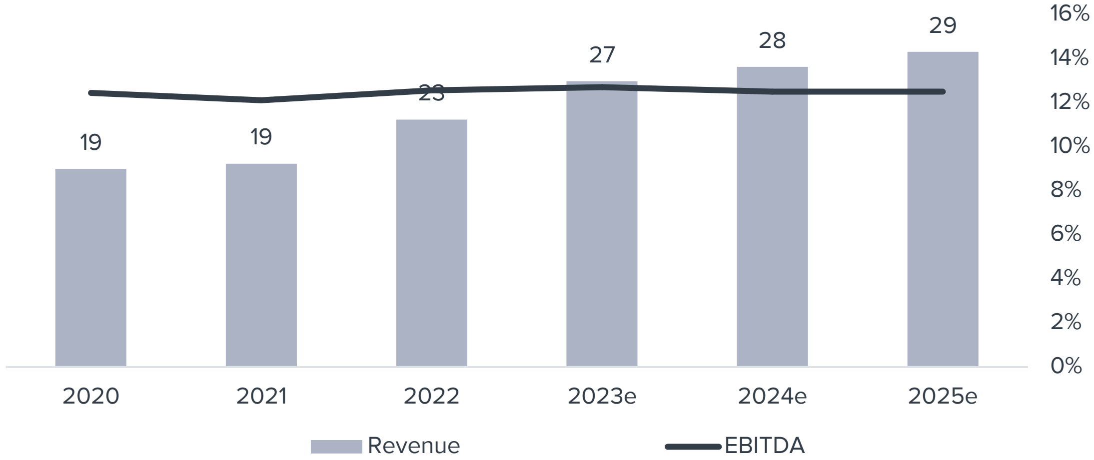
The company has a strong growth track record, and the business has grown organically by some 50% since 2017. Long-term customer relationships, skilled and committed personnel, and a strong service concept and brand form the competitive advantages of HTJ's operations.

Estimate of earnings growth rate

Value creation potential

Risk profile

Key figures and estimates:



Value drivers

- Strongly growing target market
- Continue growing stronger than the market organically
- In recent years, the biggest growth has come from infrastructure services, which continue to show significant growth potential
- Acquisitions as a growth catalyst

Risk factors

- Weakening economic situation
- Tightening competitive situation
- Failure in acquisitions

Valuation

- A clear discount to listed peers is justified due to the smaller size.
- We look at 2023 multiples as the Infrap acquisition is only then visible in full-year earnings estimates.

*The company's holding at the end of 2022 was 91.7%, but it has an option to increase its holding to 100%

Source: Inderes

Peer group valuations

Indoor Group*	EV	EV/EBITDA 22	EV/EBITDA 23	P/E 22	P/E 23
Surteco Group SE	649	7.6	7.7	10.5	24.6
Nobia AB	517	4.3	6.0	6.4	48.7
Maisons du Monde SA	1139	5.0	5.0	14.7	12.8
Leon's Furniture Ltd	1091	4.7	5.4	7.7	9.6
Williams-Sonoma Inc	1154	5.1	4.8	9.4	8.2
Median	**1091**	**5.0**	**5.4**	**9.4**	**12.8**
Indoor Group (IFRS)	119	5.0	4.8	50.6	56.5
Diff-%	-89%	0%	-11%	439%	340%

NB! Indoor's 2022 EBITDA weakened temporarily by EUR 3.2 million due to the ERP system update and we have adjusted this item in 2022 figures. We also expect around EUR 1 million of these costs in the 2023 estimate, which we have adjusted here.

HTJ	EV	EV/EBITDA 22	EV/EBITDA 23	EV/S 22
Sitowise Group Oyj	222	9.1	7.7	1.1
Sweco AB (publ)	3938	16.0	13.7	1.9
Afry AB	2031	9.9	8.4	1.0
Rejlers AB (publ)	298	9.0	8.0	1.0
WSP Global Inc	18815	18.2	14.6	3.1
Etteplan Oyj	466	9.6	9.7	1.3
Arcadis NV	4891	13.1	10.0	1.3
Median	**2031**	**9.9**	**9.7**	**1.3**
HTJ	21	7.2	6.5	0.9
Diff-%	-99%	-28%	-33%	-31%

KH-Koneet Group	EV	EV/EBITDA 22	EV/EBITDA 23	P/E 22	P/E 23
Ponsse Oyj	913	11.7	9.9	23.1	18.6
Palfinger AG	1728	7.6	6.0	12.1	8.4
Volvo AB	53856	9.4	7.5	12.1	9.0
Deere & Comp	164500	16.6	12.4	18.9	13.7
Caterpillar Inc	160255	16.8	12.0	20.5	14.3
AGCO Corp	10350	7.6	5.8	10.8	8.3
Terex Corp	4127	9.9	6.4	14.7	8.5
Median	**10350**	**9.9**	**7.5**	**14.7**	**9.0**
KH-Koneet Group	80	6.3	6.5	8.7	9.3
Diff-%	-99%	-36%	-13%	-41%	3%

Nordic Rescue Group	EV	EV/EBITDA 22	EV/EBITDA 23	EV/S 22
Rosenbauer Int AG	637	22.1	10.5	0.6
Oshkosh Corp	6391	14.7	8.3	0.9
REV Group Inc	948	10.2	8.2	0.5
Median	**948**	**14.7**	**8.3**	**0.6**
Nordic Rescue Group*	11.4	-5.7	6.0	0.3
Diff-%	-99%	-139%	-27%	-57%

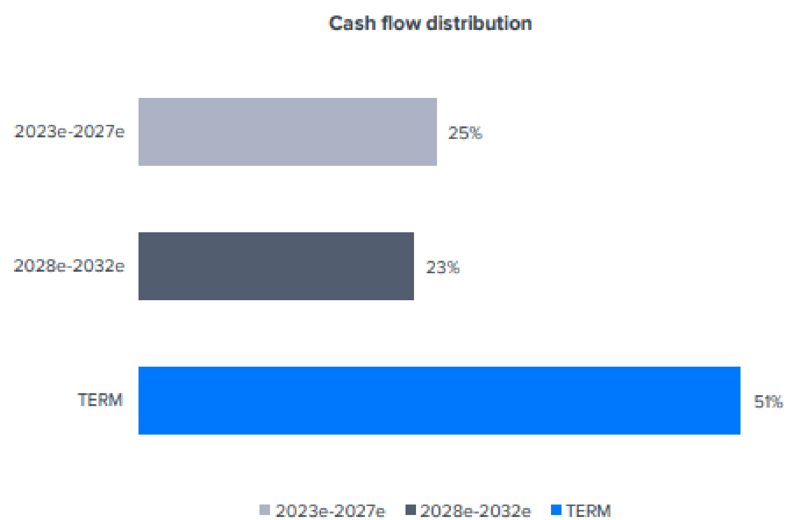
Source: Inderes and Refinitiv, valuation levels for peers collected on August 14, 2023. * Indoor Group EV includes lease liabilities under IFRS 16. Estimates of other companies under FAS accounting.

DCF calculation

DCF calculation KH-Koneet	2022	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e	2031e	2032e	TERM
Revenue growth-%	15.4 %	0.0 %	5.0 %	5.0 %	5.0 %	5.0 %	5.0 %	2.0 %	2.0 %	2.0 %	2.0 %	2.0 %
EBIT-%	4.4 %	4.2 %	4.2 %	4.7 %	4.7 %	4.8 %	4.9 %	5.1 %	5.2 %	5.2 %	5.2 %	5.2 %
EBIT (operating profit)	**8.6**	**8.1**	**8.7**	**10.2**	**10.5**	**11.4**	**12.2**	**12.9**	**13.5**	**13.7**	**14.0**	
+ Depreciation	2.9	2.3	2.0	1.8	1.7	1.6	1.5	1.5	1.4	1.3	1.3	
- Paid taxes	-2.4	-1.5	-1.5	-1.9	-2.0	-2.2	-2.4	-2.5	-2.6	-2.7	-2.6	
- Tax, financial expenses	-0.2	-0.3	-0.3	-0.3	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	
+ 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	-8.0	-2.0	-2.2	-2.4	-2.5	-2.6	-2.7	-1.1	-1.2	-1.2	-1.2	
Operating cash flow	**0.9**	**6.6**	**6.6**	**7.5**	**7.5**	**8.0**	**8.4**	**10.5**	**10.8**	**11.0**	**11.3**	
+ Change in other long-term liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
- Gross CAPEX	-0.5	-1.0	-1.0	-1.1	-1.1	-1.1	-1.1	-1.0	-1.0	-1.0	-1.4	
Free operating cash flow	**0.4**	**5.6**	**5.6**	**6.5**	**6.5**	**7.0**	**7.4**	**9.5**	**9.8**	**10.0**	**9.9**	
+/- Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
FCFF	0.4	5.6	5.6	6.5	6.5	7.0	7.4	9.5	9.8	10.0	9.9	124
Discounted FCFF		**5.2**	**4.7**	**4.9**	**4.5**	**4.4**	**4.2**	**4.9**	**4.6**	**4.2**	**3.8**	**48.0**
Sum of FCFF present value		93.5	88.3	83.6	78.7	74.2	69.8	65.6	60.7	56.1	51.8	48.0
Enterprise value DCF		**93.5**										
- Interesting bearing debt		-44.9										
+ Cash and cash equivalents		17.0										
-Minorities		0.0										
-Dividend/capital return		0.0										
Equity value DCF		**65.6**										
Equity value DCF per Sievi's share		**1.1**										

Wacc	
Tax-% (WACC)	20.0 %
Target debt ratio (D/(D+E)	20.0 %
Cost of debt	5.0 %
Equity Beta	1.30
Market risk premium	4.75%
Liquidity premium	3.00%
Risk free interest rate	2.5 %
Cost of equity	**11.7 %**
Weighted average cost of capital (WACC)	**10.1 %**

Source: Inderes



Source: Inderes. We stress to investors that our DCF calculation is indicative, as there is a long delay before the financial statements of unlisted companies become public. We have used KH's 2021 financial statements and the current net debt reported in Sievi's 2022 financial statements to derive the parameters.

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Recommendation history (>12 mo)

Date	Recommendation	Target	Share price
8/23/2019	Reduce	1.25 €	1.24 €
10/30/2019	Reduce	1.25 €	1.23 €
11/29/2019	Accumulate	1.30 €	1.21 €
1/8/2020	Reduce	1.40 €	1.40 €
1/30/2020	Reduce	1.25 €	1.35 €
3/4/2020	Reduce	1.15 €	1.18 €
4/27/2020	Reduce	0.90 €	0.87 €
4/29/2020	Accumulate	0.92 €	0.88 €
6/23/2020	Accumulate	0.98 €	0.89 €
8/26/2020	Accumulate	1.10 €	1.04 €
10/30/2020	Buy	1.15 €	1.01 €
2/25/2021	Buy	1.30 €	1.19 €
4/14/2021	Accumulate	1.55 €	1.49 €
4/30/2021	Accumulate	1.55 €	1.48 €
6/17/2021	Buy	1.65 €	1.34 €
8/18/2021	Accumulate	2.10 €	2.06 €
8/19/2021	Accumulate	2.80 €	2.39 €
9/30/2021	Buy	2.80 €	1.95 €
11/1/2021	Accumulate	2.50 €	2.09 €
12/15/2021	Accumulate	2.00 €	1.94 €
3/4/2022	Buy	1.80 €	1.52 €
3/17/2022	Accumulate	1.80 €	1.64 €
5/6/2022	Buy	1.80 €	1.36 €
8/18/2022	Accumulate	1.50 €	1.29 €
11/4/2022	Buy	1.40 €	1.14 €
12/16/2022	Buy	1.40 €	1.17 €
2/21/2023	Accumulate	1.35 €	1.20 €
3/1/2023	Accumulate	1.20 €	1.08 €
5/5/2023	Buy	1.20 €	1.03 €
8/15/2023	Buy	1.20 €	1.01 €

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2014, 2016, 2017, 2019

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2014, 2015, 2016, 2018, 2019, 2020

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