



Interim report
1 January – 30 June 1999

- Net turnover increased by 22.7 percent to MSEK 192.1 (156.5).
- Improvement in results, MSEK –14.7 (-29.4).
- Continued expected increase in average price per item of mail.
- Execution of further cost reductions to begin during the fourth quarter.
- Geographic expansion is planned.
- Settlement with Sweden Post.
- Home deliveries of parcels through ASG Direct initiated on 4 October 1999.

Revenues

During the first half of 1999, CityMail's revenues amounted to MSEK 192.1, an increase of 22.7% compared with the first half of 1998.

Sales to CityMail's existing customers increased by approximately 13%. Within the segment of major customers, existing customers accounted for 98 percent of the increase, while the increase among small and medium-size customers came almost exclusively from new sales.

Average revenues per item of mail increased by approximately 2.5 percent. The effect of the new price-lists which were introduced by CityMail on 1 April 1999 was only felt on new sales during the second quarter and thus additional increases in average revenues per item of mail can be expected during the remainder of the year.

The distribution of outbound foreign mail commenced during the second quarter and has contributed to the increase in new sales.

Revenues during the second quarter amounted to MSEK 95.2.

During the second quarter, a settlement agreement was reached with Posten. The agreement covered both CityMail's claims in damages against Posten, as well as certain claims which Posten deemed itself to have against CityMail with respect to previously provided infrastructural services. The settlement agreement resulted in net payment to CityMail, part of which was allocated to income in the second quarter. At the same time, development expenditures relating to the competition law which had been capitalised have been dissolved. A certain positive net effect has arisen during the second quarter.

Costs

CityMail's operating costs for the first half of 1999 amounted to MSEK 205.2 (184.5). The increase between the years is accounted for by the expansion of the sales organisation and an increased dimensioning of the distribution organisation which were made during 1998.

During the second quarter of 1999, operating costs amounted to MSEK 101.9, a reduction of MSEK 1.4 compared with the first quarter of 1999. Operating costs for the third quarter of 1999 are expected to be lower than the costs for the second quarter.

The programme to increase capacity utilisation efficiency, which was introduced during the first quarter, has now been supplemented with an

analysis of a modified distribution schedule. The intention is to apportion volumes more equally, whereby significant increases in capacity utilisation and thereby cost savings can be achieved. The changes will also provide the possibility for increased product differentiation. The changes will be carried out during the fourth quarter, following appropriate negotiations with the trade unions.

The measures that have been taken in order to combat the increased turnover of personnel have borne fruit and staff turnover declined during the second quarter.

Geographic expansion

On 1 July 1999, new legislation governing the postal infrastructure entered into force. On the same day, CityMail also announced a settlement agreement with Posten. The new conditions constitute a basis for CityMail to develop even more strongly than before and, accordingly, geographical expansion is now being planned. The plans cover an additional 600,000 households in Gothenburg and Malmö. The primary purpose is to increase the critical mass in these areas.

Home delivery of parcels - ASG Direct

At the end of 1998, ASG and CityMail established a jointly-owned company in order to handle the distribution of parcels which are generated via electronic and other distance trading. A pilot operation was commenced during the second quarter in the form of the distribution of perishable commodities. The full-scale distribution with both home deliveries and collection possibilities in the Greater Stockholm area is planned for 4 October of this year.

Results

CityMail's results for the first half of 1999 improved to MSEK -14.7, compared with MSEK -29.4 during the first half of 1998. The result for the period is affected by MSEK -0.5 relating to the company's minority interest in ASG Direct AB.

The operating result for the first half of the year improved to MSEK -13.1, compared with MSEK -28.0 during the first half of 1998.

The improvement in the results is directly due to the 22.7 % increase in revenues. Costs as a consequence of capacity expansion, increased sales organisation and increased mobility of

personnel have had a moderating effect on the improvement in the results.

Financial items excluding minority participations amounted to MSEK –1.1, compared with MSEK –1.5 in the preceding year.

The result per share, excluding outstanding warrants, amounted to SEK –2 (–4).

The Board of Directors is of the opinion, as previously, that the prospects are positive for a significant improvement in the results for 1999 compared with 1998.

Financial position

The company's liquid funds including non-utilised credits amounted, on 30 June 1999, to MSEK 54.4 (79.8). Cash flow amounted to MSEK 6.7 (76.9). The equity ratio per 30 June 1999 was 27.4 percent (52.7).

Managing Director's Comments

Turn of the tide

The summer of 1999 was the time when the postal markets both in Sweden and in Europe took the decisive step towards a well-functioning market. The development constitutes a significant turn of the tide for CityMail.

As we have pointed out on many occasions, it is becoming increasingly clear that integration between the IT and telecommunication markets is also providing the impetus for changes within the logistics area. The development is taking place at an ever increasing rate and also entails changes in the individual segments of the market.

One rapidly expanding segment is **computer-addressed mail**. This segment consists largely of "business-to-consumer" correspondence, where customers utilise physical mailings as an element of direct contact with customers and potential customers. This is CityMail's core area.

Being the world's first private postal company to have established large scale operations within this area, CityMail is in a favourable position. CityMail's operations utilise IT developments in order to eliminate a whole series of time- and resource-consuming activities in the logistics flow.

Capital expenditures

Capital expenditures during the period amounted to MSEK –2,2 (5.9) following the writing off of development expenditures related to competition law that had been capitalised.

Personnel

The number of employees amounted to 960 (910).

The work of implementing Balanced Scorecards has continued during the period. This procedure constitutes an important element for creating participation in the company's vision and strategy, and thereby increased profitability in the company.

An important new product area on the market for written communications is **e-mail**, which has experienced a very strong growth, primarily at the cost of traditional letter delivery within the office post segment.

An additional expanding segment is **parcel distribution**, the growth of which is primarily generated by the rapid increase in electronic commerce. Here also, City Mail is prepared thanks to its co-ownership in ASG Direct.

The analyst firm, Forrester, has recently forecast a significant increase in the digital business-to-business trade – from a turnover in 1998 of approximately 40 billion dollars to an incomprehensible 1,300 billion dollars already by 2002. During the same period, it is estimated that consumer shopping via the Internet will increase from 8 billion to 108 billion dollars.

The great increase in electronic trading places a high demand on the functions which must attend to the logistics of the trading. Speed, flexibility, and the ability to integrate into existing digital systems will become major competitive factors vis-à-vis other logistics companies in this development.

This is also the reason for our alliances and co-operations with, for example, Royal Mail and ASG, in which we, as a small branch player in

Sweden, can operate across branches and borders.

New situation in Sweden

In light of the increasingly clear global trends it is thus heartening to note that the Swedish postal market has once again taken the lead in the process of deregulation.

Commencing on 30 June 1999, a new and clearer legislative regime applies to the postal area. The new Postal Services Act clarifies the infrastructure on the market in which we operate and places limits as to how the various participants can, and must, function together.

At the same time, it was publicly announced that a settlement agreement had been reached between CityMail and Posten. This means that a relatively turbulent period in Posten's and CityMail's history is now over.

The new legislation, the settlement with Posten, and the new management in Posten, have meant that our relations with the Swedish Postal Service are now normalised in a healthy manner.

Positioning for future deregulation.

The development is now about to fundamentally change not only for the Swedish, but also the European, postal market. Major international players, fearing that they will not have time, are now positioning themselves ever more clearly in order to maintain market shares in the future deregulated European market.

This positioning is important for CityMail in two respects.

Firstly, the struggle between the major monopolies in Europe means increased pressure on decision-makers to carry out deregulation. In a newly issued number of the *Post-express* bulletin, Hubert Ungerer, head of the postal unit in the EU Commission's competition division, states: "I would not be astonished if the Commission would be basically obliged to start, at

least for those companies that have the most aggressive expansion policies, a re-examination of their monopoly".

Things could not be stated more clearly. Within the EU Commission, there is a limit as to how aggressive the monopolies may be in their cross-border activities in Europe. Accordingly, the activities of the current monopolies to position themselves pending future deregulation also contribute, at the same time, to an acceleration of the deregulation procedure.

The new majority in the EU Parliament will probably also strengthen this position and further advance the deregulation work on the European postal market.

Secondly, international structural transactions are taking place which directly affect CityMail. For example, ASG is now considered to be in the process of being acquired by Deutsche Post. CityMail, which together with ASG owns ASG Direct, is following this matter with great interest.

Faced with future international changes, Sweden and CityMail represent the sole working examples of how a deregulated postal market functions. The ten years of our existence can be regarded as one major investment in logistics, systematics, legal infrastructure and the creation of an entirely new market.

I will gladly admit that, at times, these have been very difficult years. At the same time, it is extremely satisfying to be able to note that the efforts have borne fruit and that our know-how and collective experience are now attractive on the market. Our "business-model" is proven, and we have built an entirely new market from the ground up. Quarrels on the Swedish postal market are now over. The basis has been laid for international expansion. Now we are ready to harvest the fruits of our investments.

Bror Anders Månsson
Managing director

This interim report has not been the subject of an audit by the company's auditors.

Stockholm 11 August 1999



Interim report

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An analysts meeting will be held at Operaterassen in Stockholm on 12 August 1999 at 07:45 a.m.

Future reports

Interim report, 9 months
8 November

Press release of un-audited 1999 results February 2000

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