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Annual Report 2012

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Markets and Digia’s business operations

The current weak economic prospects have from time to time caused delays in customers’ decision-making and therefore in the start-up of new projects. Additionally, constant cost pressures on customers are reflected in their procurement decisions.

The human resources situation has two quite different aspects. On the one hand, a large number of experts were released onto the job market from various contract engineering projects; on the other, there is a shortage of experienced architecture and business experts, which is causing lengthened recruitment processes and pressure for pay rises.

The company’s new organisation took effect at the beginning of 2012. It proved to be effective and worked according to plan. In some areas, operational efficiency will be enhanced further to improve profitability and develop the service portfolio.

The increased cost pressure on Digia’s customers particularly affected demand for customer-specific solutions and services during the financial year, especially in the private sector.

Demand for ERP systems and other operational systems was fair during the review period, although increased caution was evident in customers’ purchasing behaviour and sales cycles had become longer. The order intake book was still at a normal, healthy level.

The Qt business increased its net sales, with operations progressing according to plan during the period. The high profitability of the business fell towards the end of the review period, as expected, due to the Nokia Qt deal increasing the costs of the business. During the period the company revised some of its previously published plans related to Qt product development and its areas of focus. The new Qt message was positively received by the market and has opened significant new business opportunities, especially in the large customer segment.

In Digia’s Russian unit, the focus of business development was on ERP system solutions for local customers within the retail value chain. Besides offering services locally, the Russian unit also supports the company’s business in Finland by providing near shore services, particularly within ERP system solutions.

The focus of development of the Chinese unit was increasingly on Qt licence and consulting services offered to the local Chinese market. The completed Qt acquisition reinforced the company’s competitiveness in this area.

Financial Indicators

The group’s operations were profitable, resulting in an operating profit of EUR 6.9 million. The group maintained good solvency and liquidity. Consolidated financial indicators are presented in the following table:

	2012	2011	2010	2009	2008
Net Sales	100,448	121,940	130,825	120,335	123,203
EBIT	6,884	-22,168	17,164	-7,796	13,437
Operating margin, %	7%	-18%	13%	-6%	11%
Return on equity, %	10%	-42%	18%	-21%	11%
Equity ratio, %	53%	48%	59%	52%	47%
Net gearing, %	28%	34%	20%	34%	53%

More detailed key figures for the last five years and the formulae for the key figures are provided in the notes to the financial statements (Note 30).

Net Sales

Digia's consolidated net sales for the fiscal year were EUR 100.4 (121.9) million, down 17.6 per cent on the previous year.

The decrease was due to a sharp fall in demand for mobile contract engineering services from Q2 2011 onwards, which continued through 2012. Net sales generated by the Qt business grew significantly from the comparison period, reaching EUR 18.3 million during the period under review. Of that figure, EUR 4.2 million came from the granting of rights of use of Qt technology to Nokia as part of the Qt business acquisition.

During the financial year, the product business accounted for EUR 36.5 (25.7) million or 36.4 (21.0) per cent of consolidated net sales.

International operations accounted for EUR 20.6 (14.7) million or 20.5 (12.1) per cent of consolidated net sales.

Profitability and Financial Performance

Digia's consolidated operating profit before extraordinary items for the reporting period was EUR 8.2 (8.1) million, up 1.4 per cent year on year. Profitability (EBIT%) before extraordinary items was 8.2 (6.6) per cent.

Digia's consolidated operating profit after extraordinary items for the review period was EUR 6.9 (-22.2) million. Profitability (EBIT%) after extraordinary items was 6.9 (-18.2) per cent. Extraordinary items comprised a EUR 1.3 million restructuring cost related to the personnel negotiations and reorganisations conducted during the year.

Operating profit and profitability were positively affected in the review period by income from the granting of rights of use of Qt technology to Nokia as part of the Qt deal. Conversely, the company's operating cost structure and profitability were negatively affected during the period by investments into the international product business and a relative increase in the proportion of fixed operating costs. There were also temporary negative effects from the additional costs caused by increased personnel turnover at the beginning of the year, and by loss provisions related to two customer projects in the third quarter. The profitability of the Solutions and Services business was lower than expected throughout the period.

Consolidated earnings before tax for the year totalled EUR 5.6 (-23.1) million, and net profit was EUR 4.0 (-22.5) million.

Consolidated earnings per share for the review period totalled EUR 0.26 (0.32) before extraordinary items and EUR 0.19 (-1.08) after extraordinary items.

The Group's net financial expenses for 2012 were EUR 1.3 (1.0) million.

Financial Position and Expenditure

At the end of the reporting period, Digia Group’s consolidated balance sheet total stood at EUR 92.4 million (12/2011: EUR 87.8 million), and the equity ratio was 52.6 (47.8) per cent. Net gearing was 27.5 (34.5) per cent. Period-end cash and cash equivalents totalled EUR 8.3 (8.2) million.

Interest-bearing liabilities amounted to EUR 19.8 (21.9) million at the period end. These consisted of EUR 18.5 million in loans from financial institutions and EUR 1.3 million in financial leasing liabilities.

To finance its Qt business acquisition, Digia took out EUR 4.0 million in a long-term loan on 17 September 2012. The loan covenants of the financing package agreed in 2011 remained unchanged. The loan covenants related to the company’s solvency and liquidity comprised the following key figures: operating profit before depreciation and amortisation (EBITDA) in relation to net debt, equity ratio and net gearing. The company may distribute a maximum of 50 per cent of the Group’s net profit for the year without separate agreement. The company fulfilled the set loan covenants in 2012. Further information on financing loans is presented in Note 22 to the financial statements.

The Group carries out quarterly impairment testing of goodwill and intangible assets with an indefinite useful life. Impairment testing is described in more detail in the notes to the financial statements, under Note 15 ‘Intangible assets’.

The company has financing, framework and delivery agreements with special terms and conditions for any situation in which control of the company changes hands.

The Group's cash flow from business operations for 2012 was positive by EUR 19.9 (8.8) million, cash flow from investments was negative by EUR 16.2 (2.7) million and cash flow from finance was negative by EUR 3.6 (7.6) million. Billing of EUR 12.2 million from Nokia in relation to the Qt acquisition deal had a positive impact on operational cash flow. Cash flow from finance was negatively affected by a repayment of loans totalling EUR 5.5 million, as well as by the payment of dividends with a total effect of EUR 2.1 million. Additionally, a long-term loan of EUR 4.0 million was taken out for the Qt acquisition.

The Group’s total investments into fixed assets were EUR 0.8 (2.7) million. Acquisitions of tangible fixed assets totalled EUR 0.7 (2.3) million.

Return on investment (ROI) for the financial year was 11.3 (-28.7) per cent and return on equity (ROE) was 9.8 (-41.9) per cent.

Extent of Research and Development

The Group made research and development efforts and engaged in product development in all of its divisions. In the 2012 fiscal year, the Group’s R&D costs totalled EUR 4.3 million (2011: EUR 4.8 million and 2010: EUR 4.8 million), corresponding to 4.2 per cent of net sales (3.9 per cent and 2.3 per cent).

Personnel, Management and Administration

At the end of the period, the total number of Group personnel was 982, representing a decrease of 193 employees or 16.4 per cent compared to the end of 2011 (1,175). During the reporting period the number of employees averaged 1,025, a decrease of 428 employees or 29.5 per cent from the 2011 average (1,453).

Employee indicators:

	2012	2011	2010
Average number of personnel	1,025	1,453	1,508
Wages and salaries	54,028	68,564	65,172

Employees by function, year-end 2012:

Business units	96%
Administration and management	4%

As of the end of the period, 195 (12/2011: 161) employees were working abroad.

The Digia Plc Annual General Meeting of 13 March 2012 re-elected Robert Ingman, Kari Karvinen, Pertti Kyttälä and Tommi Uhari as members of the Board. Päivi Hokkanen, Seppo Ruotsalainen and Leena Saarinen were elected as new members. At the organisation meeting of the Board, Pertti Kyttälä was elected Chairman of the Board and Robert Ingman Vice Chairman.

Juha Varelius has been Digia Plc’s President and CEO since 1 January 2008.

Anja Wasenius started as Acting CFO in June 2012.

In 2012, Digia’s Board of Directors had three committees: the Compensation Committee, the Audit Committee, and the Nomination Committee. The Board approved the rules of procedure for 2012 of the committees in a meeting of 29 March 2012.

These committees do not hold powers of decision or execution; their role is to assist the Board in decision-making concerning their areas of expertise. The committees report regularly on their work to the Board, which has decision-making and collegial responsibility over their actions.

The Compensation Committee's task is to prepare and follow management remuneration schemes in order to ensure that the company's targets are met, that the objectivity of decision-making is maintained, and that the schemes are transparent and systematic. In 2012, the Compensation Committee comprised Tommi Uhari (chairman), Robert Ingman and Päivi Hokkanen. Until the 2012 AGM, the Committee’s members were Martti Mehtälä (chairman), Pekka Sivonen and Tommi Uhari. The committee convened four times in 2012, with full attendance.

The purpose of the Audit Committee is to assist the Board of Directors in ensuring that the company's financial reporting, accounting methods, financial statements and other financial information provided by the company are in accordance with the law, balanced, transparent and clear. In 2012 the Audit Committee was made up of Pertti Kyttälä (Chairman), Kari Karvinen, Seppo Ruotsalainen and Leena Saarinen. Until the AGM, the members were Pertti Kyttälä (Chairman), Kari Karvinen and Marjatta Virtanen. The committee convened five times in 2012, with full attendance.

The Nomination Committee will prepare proposals for the Annual General Meeting of the shareholders concerning (a) the number of members of the Board of Directors, (b) the members of the Board of Directors, (c) the remuneration for the Chairman, Vice Chairman and members of the Board of Directors and (d) the remuneration for the Chairman and members of the committees of the Board of Directors. In 2012, the Nomination Committee members were Robert Ingman (chairman), Kari Karvinen and Pertti Kyttälä. The committee convened four times with full attendance.

Ernst & Young Oy, authorised public accountants, are the Group’s auditors, with Authorised Public Accountant Heikki Ilkka as the principal auditor.

Digia adheres to the Governance Code for Listed Finnish Companies, issued on 1 October 2010 by the Finnish Securities Market Association. Digia’s corporate governance system is based on the Companies Act, the Securities Markets Act, general corporate governance recommendations, and the company’s Articles of Association and in-company rules and regulations on corporate governance. The Governance Code and a separate review of the Group's corporate governance and management system made for this annual report can be seen at www.digia.com.

Business Acquisitions

On 8 August the company made a deal to buy Qt software technology and the related business from Nokia Plc. With the acquisition, 88 employees in Norway, Germany and Finland were transferred to the company's employ. The deal became effective on 18 September 2012 and the net acquisition price was EUR 4.0 million, comprising the sale price of EUR 16.2 million related to the assets and business transferred, minus a bill of EUR 12.2 million from Digia to Nokia.

Of the sale price of EUR 16.2 million, EUR 6.6 million of goodwill pertained to intangible rights, EUR 2.9 million to the brand, EUR 4.1 million to technology and EUR 1.0 million to the customer relationship with Nokia. In line with the Finnish financial reporting standard, the recorded depreciation from goodwill is tax-deductible. Additionally, EUR 0.2 million was recorded as an expense and EUR 1.5 million as a loan repayment related to an expense from 2012 covered as a part of the deal.

Group Structure and Organisation

At the end of the year, the Digia Group consisted of parent company Digia Plc and its active subsidiaries Digia Finland Ltd (parent company holding 100%); Digia Sweden AB (100%); Digia Estonia Oü (100%), Digia Hong Kong Ltd (100%), Digia Norway AS (100%), Digia USA Inc. (100%), and Digia Germany GmbH (100%). Digia Partners Ltd (100%) merged into Digia Plc on 31 October 2012.

Digia Finland Ltd has one wholly owned active subsidiary, OOO Digia RUS. Digia Finland Ltd’s former wholly owned subsidiaries Digia Financial Software Ltd, Digia Service Ltd and Microext Ltd merged into their parent on 31 October 2012.

Digia Hong Kong Ltd has the wholly owned subsidiary Digia Software (Chengdu) Co. Ltd (100%), with a registered branch in Beijing. Digia Estonia Oü and Digia Hong Kong Ltd are inactive.

Towards the end of 2011, the company carried out a reorganisation which came into effect at the start of 2012. In the new organisation, business is managed according to four strategic portfolios: Solutions and Services, Industry-Specific Growth Businesses, International Product Business, and New Markets (e.g. Russia).

Shareholders' Meetings

Convening on 13 March 2012, the Digia Plc Annual General Meeting (AGM) approved the financial statements for 2011, released the Board members and the CEO from liability, determined Board emoluments, resolved to keep the number of Board members at seven, and elected the Board of Directors for the new term.

With regard to profit distribution for 2011, the AGM approved the Board's proposal to make a repayment of capital of EUR 0.10 per share to all shareholders listed in the shareholder register maintained by Euroclear Finland Ltd on the reconciliation date of 16 March 2012. The date for the repayment of capital was 23 March 2012. The AGM granted the following authorisations to the Board:

Authorisation of the Board of Directors to decide on buying back own shares and/or accepting them as collateral

The AGM authorised the Board to decide on the buyback and/or acceptance as collateral of not more than 2,000,000 shares in the company. This buyback can only be executed by means of the company's unrestricted equity. The Board shall decide on how these shares are to be bought. Own shares may be bought back in disproportion to the holdings of the shareholders. The authorisation also includes acquisition of shares through public trading organised by NASDAQ OMX Helsinki Ltd in accordance with the rules and instructions of NASDAQ OMX Helsinki and Euroclear Finland Ltd, or through offersmade to shareholders. Shares may be acquired in order to improve the company's capital structure, to fund acquisitions or other business transactions, for offering share-based incentive schemes, to sell on, or to be annulled. The shares must be acquired at the market price in public trading. This authorisation supersedes that granted by the AGM of 16 March 2011 and is valid for 18 months, i.e. until 13 September 2013.

Authorising the Board of Directors to decide on a share issue and granting of special rights

The AGM authorised the Board to decide on an ordinary or bonus issue of shares and the granting of special rights (as defined in Section 1, Chapter 10 of the Limited Liability Companies Act) in one or more instalments, as follows: The issue may total, at a maximum, 4,000,000 shares. The authorisation applies both to new shares and to treasury shares held by the company. By virtue of the authorisation, the Board has the right to decide on share issues and the granting of special rights, in deviation from the pre-emptive subscription rights of the shareholders (a directed issue).

The authorisation may be used to fund or complete acquisitions or other business transactions, for offering share-based incentive schemes, to develop the company's capital structure, or for other purposes. The Board was authorised to decide on all terms related to the share issue or special rights, including the subscription price, its payment in cash or (partly or wholly) in capital contributed in kind or its being written off against the subscriber's receivables, and its recognition in the company's balance sheet. This authorisation supersedes that granted by the AGM of 16 March 2011 and is valid for 18 months, i.e. until 13 September 2013.

Share Capital and Shares

The nominal share price is EUR 0.10. The number of shares at the end of 2012 totalled 20,875,645. At the year-end, the company held 103,122 of its own shares.

On 31 December 2012, according to Finnish Central Securities Depository Ltd, Digia had 5,770 shareholders.

The 10 biggest shareholders on 31 December 2012

Shareholder	Percentage of shares and votes
Ingman Group Oy Ab	16.8%
Jyrki Hallikainen	10.2%
Pekka Sivonen	8.8%
Kari Karvinen	6.3%
Matti Savolainen	6.1%
Ilmarinen Mutual Pension Insurance Company	4.8%
Varma Mutual Pension Insurance Company	3.6%
Nordea Bank Finland Plc (nominee-registered)	1.6%
Etola Oy	1.0%
Rausanne Oy	0.9%

Distribution of holdings by number of shares held on 31 December 2012

Number of shares	Percentage of holdings	Percentage of shares and votes
1 - 100	22.4%	0.4%
101 - 1,000	58.7%	7.4%
1,001 - 10,000	17.4%	12.9%
10,001 - 100,000	1.1%	8.8%
100,001 - 1,000,000	0.4%	22.4%
1,000,001 - 3,000,000	0.1%	48.1%

Shareholding by sector on 31 December 2012

	Percentage of holdings	Percentage of shares and votes
Non-financial corporations	4.5%	22.0%
Financial and insurance corporations	0.2%	4.8%
General government	0.1%	8.4%
Not-for-profit institutions serving households	0.2%	0.5%
Households	94.6%	63.2%
Rest of the world	0.4%	1.1%

Share-based Payments

Stock options

Digia Plc had no outstanding options at the time of writing.

Share incentive scheme and management ownership

The company has a share bonus system as a part of its key personnel commitment and incentive scheme. With authorisation received at the AGM, the Board made a decision on the CEO's share-based incentive scheme in spring 2010.

The scheme comprises four earning periods, which are the calendar years 2010–2013. According to the scheme, rewards totalling a maximum value equivalent to 100,000 shares will be paid for each of the earning periods from 2011 to 2013, based on the fulfilment of earning criteria set by the Board. For 2013 the reward will be determined based on the company's earnings per share and net sales, according to principles set separately by the Board.

Based on the aforementioned scheme, the CEO was paid a reward equivalent to the value of 39,266 shares in 2012, based on the results from 2011. The bonus was paid in the form of shares held by the company.

In addition to the CEO, the scheme applies to the company's other management team members, who are entitled to share the same share bonus that the CEO receives.

A sum equivalent to the value of 34,376 shares was paid to specified key personnel of the company during the financial year. The rewards are paid in four equal instalments between 2010 and 2013, based on the results from 2009.

All bonuses are paid as a 50/50 combination of shares and cash. The cash portion of the bonus is primarily used to cover taxes and other comparable costs of the scheme. The system involves no vesting periods limiting the sale of shares.

The payment of bonuses according to the share-based incentive schemes is subject to the employee in question being employed by the company on the payment date.

According to the list of shareholders dated 31 December 2012, Digia's Board of Directors and CEO owned shares in the company as follows:

Pertti Kyttälä	0
Robert Ingman	20,000
Kari Karvinen	1,309,912
Tommi Uhari	0
Juha Varelius	167,258
Päivi Hokkanen	8,170
Seppo Ruotsalainen	0
Leena Saarinen	0

At the year-end, the shares held by the Board members and the CEO represented 7.1% of the company's shares and votes.

Reported Share Performance on NASDAQ OMX Helsinki in 2012

Digia Plc shares were in 2012 listed on the Nordic Exchange under Information Technology IT Services. The company's short name is DIG1V. The lowest reported share quotation was EUR 2.28 and the highest was EUR 3.30. The share closed at EUR 2.62 on the last trading day. The trade-weighted average was EUR 2.82. The Group's market capitalisation at the year-end was EUR 54,694,190.

The company received no flagging notifications during the reporting period.

Risks and Uncertainties

The main operational risks monitored under Digia's risk management are related to customers, personnel, projects, data security, integration, incorporeal rights and goodwill.

Short-term uncertainties are related to any major changes occurring in the company's core business areas.

Contrary to previous years, the company no longer has any business risk related to mobile contract engineering services. Instead, the company made a significant investment into Qt technology and related business opportunities with the Qt business acquisition completed in 2012. If the Qt business fails to develop according to the company's expectations, the investments and related costs may have a significant impact on the company's short-term profitability. Possible changes in the competitive scenario or market for that business may also impact the company's future net sales and profitability.

If the Eurozone debt crisis and global economic recession continue, they may affect customers' investment decisions and liquidity, and thereby the company's sales and profits. Increased uncertainty has already been detected in customers' investment decisions, having delayed planned project schedules for a while, but recent developments have not been in any way alarming.

Furthermore, the growth in customer project sizes increases the risks related to projects and their profitability.

Risks and their management are described on the company's website at www.digia.com.

Future Prospects

The company is focusing heavily on paving the way for growth. Besides organic growth, the company will actively pursue opportunities to make carefully considered business acquisitions that support its strategy. The main cornerstones of the company's operations are still high profitability and a positive cash flow.

The company expects the IT market to remain at roughly the previous year's level in 2013.

Efforts will continue to be made to develop the company's sales and service portfolio to ensure that it can offer increasingly competitive services and solutions for boosting its customers' business efficiency.

The company expects demand for its ERP systems, operational systems and integration services to remain good, although increased caution on the customer side and lengthening sales cycles may have an effect on future order intake.

The company continues to seek growth in the expanding Russian market. The Chinese unit will focus on Qt licence sales and supporting service.

The company expects net sales from the Qt business to continue growing.

Operating profit is predicted to remain somewhat below normal or at most slightly positive through the first quarter of 2013, after which it should improve. Profitability is expected to return to a good level in the second half of 2013, thanks to completed streamlining measures and the development of the Qt business.

The company expects its net sales for 2013 to remain roughly at the 2012 level. Growth in net sales will be hampered by the cessation of mobile contract engineering operations.

Major Events after the Balance Sheet Date

There have been no significant events after the end of the financial year.

Board’s Dividend Proposal

According to the financial statements for 31 December 2012, the distributable shareholders’ equity of Digia Plc was EUR 36,643,688.90, of which EUR 3,558,364.21 was the net profit for the year. At the Annual General Meeting, the Board of Directors will propose that a dividend of EUR 0.10 per share be paid according to the confirmed statement of financial position for the fiscal year ending 31 December 2012. Shareholders listed in the shareholder register maintained by Euroclear Finland Ltd on the dividend reconciliation date, 15 March 2013, will be eligible for the payment of dividend. Dividends will be paid on 22 March 2013.

Digia Plc

Valimotie 21
FI-00380 Helsinki, Finland
www.digia.com