

CREDIT OPINION

13 June 2022

Update



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RATINGS

Essity Aktiebolag

Domicile	Sweden
Long Term Rating	Baa1
Type	LT Issuer Rating - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Essity Aktiebolag

Update following rating affirmation

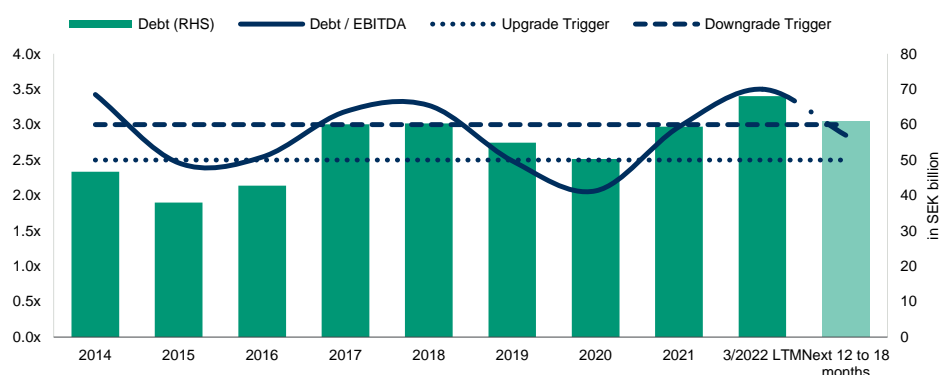
Summary

[Essity Aktiebolag's](#) (Essity) Baa1/P-2 ratings with a stable outlook primarily reflect the company's large scale, with revenue of SEK129 billion for the 12 months that ended March 2022 (around \$14.6 billion), and a broad product portfolio; its leading market positions, with well-recognised brands and a good track record of innovation; its global footprint, with the faster-growing emerging markets representing roughly one-third of its revenue; the fairly good underlying growth and the stable demand for its products; its financial policies, which are aimed at protecting its solid investment-grade rating; and Essity's track record of generating significant positive free cash flow (FCF), which it tends to use for tuck-in acquisitions and can be used to reduce leverage, if needed.

Essity's ratings are primarily constrained by its exposure to volatile input costs, pulp in particular, which can be passed through only with a significant delay; its somewhat below-average profitability compared with that of most of its similarly rated peers, such as [Kimberly-Clark Corporation](#) (K-C, A2 stable) or [The Procter & Gamble Company](#) (P&G, Aa3 stable), with a Moody's-adjusted EBITA margin of 10.0% for the 12 months that ended March 2022; and a certain degree of debt-funded M&A risk, which, however, falls within the company's commitment to maintaining a solid investment-grade rating (see Exhibit 1 below).

Exhibit 1

We expect Essity's leverage to move back into the range expected for the Baa1 rating category within the next 12-18 months



All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

The forward view represents Moody's view and does not incorporate any material divestments and acquisitions.

Source: Moody's Financial Metrics™

Credit strengths

- » A strong business profile, with a broad portfolio of well-positioned global (Tork and Tena) and regional brands
- » Fairly good underlying growth and stable demand for most of its products
- » A financial policy that is aimed at protecting its solid investment-grade rating

Credit challenges

- » Exposure to volatile input costs, such as for pulp and recycled paper
- » Ongoing need for innovation in the personal care and tissue businesses to preserve pricing levels
- » Professional care product demand hurt by the coronavirus pandemic-related lockdowns and restrictions
- » Event risks, such as debt-funded M&A or shareholder-friendly actions

Rating outlook

The stable rating outlook reflects our expectation that Essity's strong market position will enable the company to pass-on the rising input cost to its customers and to manage cost and thus to strengthen credit metrics back into the range Moody's expects for the Baa1 rating category. In addition, credit metrics will benefit from full-year contribution of recent acquisitions.

Factors that could lead to an upgrade

- » EBIT margin consistently above 12% in the company's business areas
- » Retained cash flow/net debt above 25%
- » Debt/EBITDA well below 2.5x
- » Continued positive FCF, which is applied towards debt reduction

Factors that could lead to a downgrade

- » EBIT margin remaining below 9%
- » Retained cash flow/net debt below 20% on a sustained basis
- » Inability to reduce leverage below 3.0x debt/EBITDA
- » FCF turning negative
- » Erosion of the company's solid liquidity

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

Key indicators

Exhibit 2

Essity Aktiebolag [1][2]

	2017	2018	2019	2020	2021	LTM Mar-2022 [3]	Next 12-18 months [4]
Revenue (SEK billion)	109.2	118.5	129.0	121.8	121.9	128.6	140 - 145
Revenue (USD billion)	\$12.8	\$13.6	\$13.7	\$13.3	\$14.2	\$14.6	\$15.9 - 16.5
EBIT Margin %	11.4%	9.7%	11.3%	13.7%	10.4%	8.9%	9.0% - 11.5%
EBITA Margin %	12.2%	10.5%	12.2%	14.7%	11.3%	10.0%	10.0% - 12.5%
Debt / EBITDA	3.2x	3.3x	2.5x	2.1x	3.0x	3.5x	2.7x - 3.0x
RCF / Net Debt	24.7%	20.0%	22.0%	29.6%	19.4%	9.3%	20% - 25%
FCF / Debt	10.5%	3.0%	14.9%	10.9%	1.9%	-5.0%	3% - 10%
EBITA / Interest Expense	9.0x	8.2x	10.2x	15.2x	15.4x	13.6x	13x - 17x

[1] All figures and ratios are calculated using Moody's estimates and standard adjustments.

[2] Periods are Financial Year-End unless indicated. LTM = Last Twelve Months.

[3] Adjusted for the timing of dividend payment we calculate leverage of 3.3x Debt / EBITDA, retained cash flow coverage of 18.1% RCF / Net Debt and FCF/Debt of 2.2% for the 12 months that ended in March 2022.

[4] Moody's Forecasts are Moody's opinion and do not represent the views of the issuer.

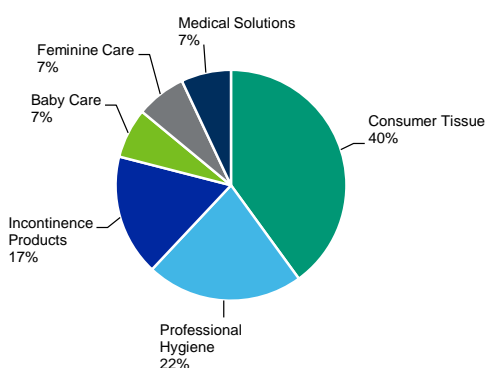
Source: Moody's Financial Metrics™, Moody's Investors Service estimate

Profile

Headquartered in Stockholm, Sweden, Essity Aktiebolag (Essity) is one of the leading global hygiene and health companies, with sales of SEK129 billion for the 12 months that ended March 2022 (around \$14.6 billion). The company develops, produces and sells a wide range of products, including incontinence products, baby diapers, feminine care products, consumer tissue, away-from-home tissue, and products for wound care, compression therapy and orthopaedics. With a workforce of roughly 46,000 employees, Essity operates in about 150 countries worldwide under a number of well-recognised brands. Essity was formed in 2016 and spun off in June 2017 from Svenska Cellulosa Aktiebolaget (SCA). The company is listed on the Stockholm Stock Exchange, with a market capitalisation of around SEK180.9 billion as of 8 June 2022.

Exhibit 3

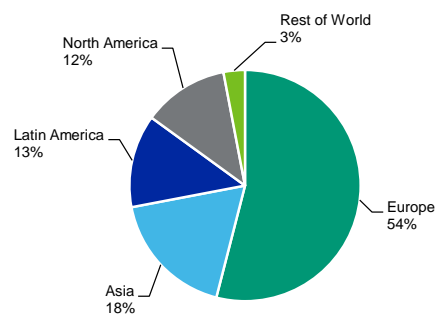
Revenue split by product As of full year 2021



Source: Essity Annual Report 2021

Exhibit 4

Revenue split by geography As of full year 2021



Source: Essity Annual Report 2021

Detailed credit considerations

Wide product portfolio, with a number of leading positions globally

Essity's Baa1/P-2 ratings reflect the company's strong market position as one of the leading global hygiene and health companies, active in around 150 countries, with sales of close to SEK130 billion. Among others, the company is the global leader in incontinence

products under the Tena brand and in professional hygiene under the Tork brand. In addition, the company has strong brands and market positions within the markets for baby diapers, feminine care and consumer tissue, as well as regional and global brands. Essity also has leading market positions in wound care, compression therapy and orthopaedics, with brands such as Jobst and Leukoplast. Overall, the company holds the first or second position within at least one product segment in around 90 countries.

Exhibit 5

Overview of market positions and key brands

	Global	Europe	North America	Latin America	Asia	Key Brands
Incontinence Products	#1	#1	#4	#1	#3	Tena
Baby Care	#5	#2	n.a.	#6	#6	Drypers, Pequenín, Libero, Lotus Baby
Feminine Care	#5	#3	n.a.	#1	#10	Libresse, Saba, Nosotras, Bodyform, Nana
Medical Solutions	#4	#1	#12	#3	#2	Jobst, Leukoplast, Cutimed, Delta-Cast, Actimove
Consumer Tissue	#2	#1	n.a.	#3	#1	Plenty, Tempo, Regio, Zewa, Lotus, Vinda
Professional Hygiene	#1	#1	#2	#4	#3	Tork

Source: Essity Annual Report 2021

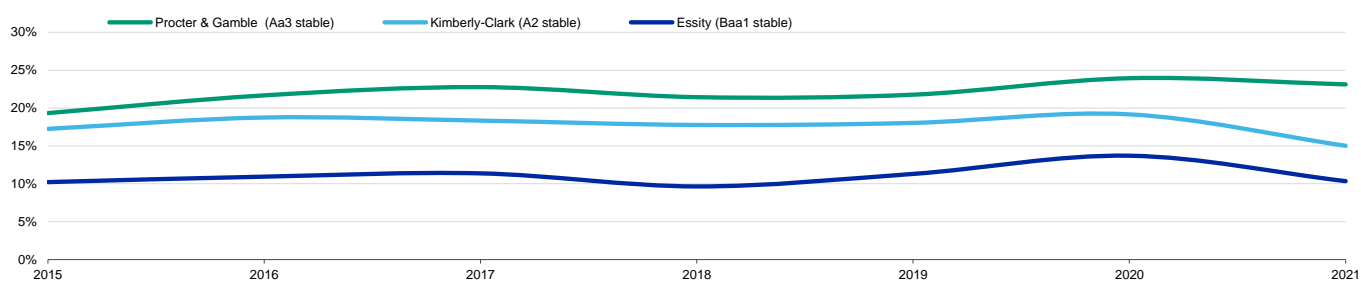
The personal care and tissue markets are fairly competitive and subject to periods of temporary oversupply, which require producers to continuously focus on innovation to protect brand strength and optimise costs. In the tissue business, which is generally more competitive and less profitable, Essity competes primarily with [Georgia-Pacific LLC](#) (A3 stable), Hengan International Group Company Limited, K-C and Sofidel S.p.A. In the personal care business, Essity's key competitors are K-C, P&G and Unicharm Corporation. In 2017, following the debt-funded acquisition of BSN Medical for €2.7 billion, the company entered the market for medical devices with low technology content, such as wound care and compression therapy, which benefits from robust and stable demand and above-average profitability.

We expect Essity to focus on growing its personal care and medical device product offerings while further increasing the efficiency of its tissue operations. In this context, Essity acquired additional shares in Asaleo Care Ltd. (Asaleo Care) and Productos Familia S.A. (Familia), during the first half of 2021, for a total cash consideration of around SEK9.4 billion, which was partially debt-funded. This strategy will help narrow the profitability gap with the company's more-profitable competitors, especially K-C and P&G, which benefit from a higher share of the more-profitable personal care business and the generally more-profitable US market.

Exhibit 6

Essity's margins have been below those of its main competitors

Moody's-adjusted EBIT margin



All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

Source: Moody's Financial Metrics™

Good underlying demand growth, especially in emerging markets

Essity benefits from the underlying growth in demand for its products, supported by megatrends such as population growth and higher disposable income, as well as the increased prevalence of people with chronic diseases. While mature markets continue to record modest annual growth in the low-single-digit percentages, the growth potential in emerging markets is substantial, and we estimate that the annual growth in these markets will be in the high-single-digit percentages. This is because the per capita consumption of tissue and personal care products in emerging markets is significantly lower while living standards are rapidly improving.

To benefit from this development, Essity focused on growing its presence in emerging markets over the past decade. This was done both organically and through M&A, most notably through the acquisition of a majority stake in the tissue company Vinda — based in Hong Kong SAR, China — in November 2013, along with the recent stake increase in Asaleo Care and Familia. In 2021, emerging markets represented 36% of Essity's net sales, and we expect this share to increase further.

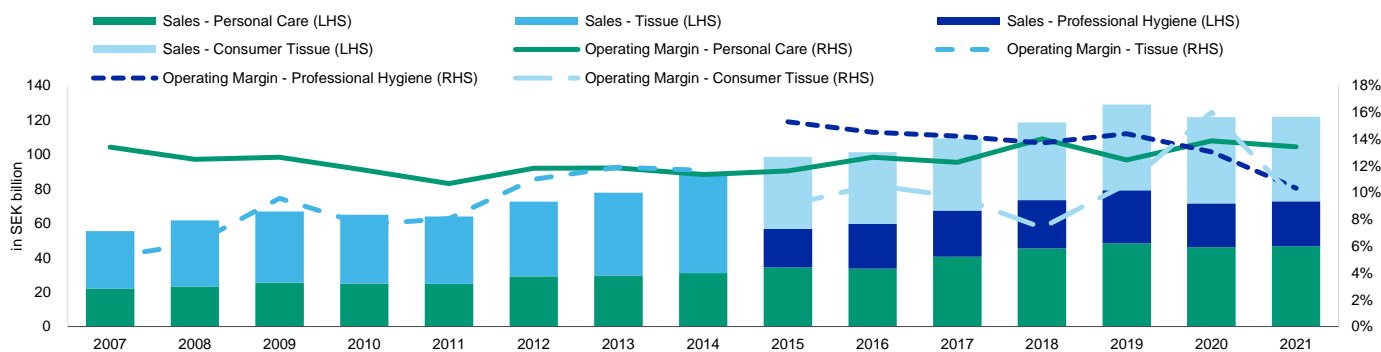
Profitability exposed to volatile input costs

The demand for Essity's products has historically been fairly stable through the cycle. Even during the 2008-09 global economic downturn, which was unprecedented in its magnitude, the company hardly faced any decline in organic sales, and the margins for both the tissue and personal care businesses, the latter one in particular, remained robust. Nevertheless, the coronavirus pandemic significantly hurt demand for professional hygiene products because of the resulting lockdown measures by governments. This prevented consumers from purchasing services as usual because larger events were cancelled and restaurants were shut down. However, the continued increase in demand for tissue products indicates an ongoing megatrend towards the increasing use of hygiene products, although it was temporarily normalised during H1 2021 when revenue in the consumer tissue segment declined by 9% compared with H1 2020 driven by lower prices and the fact that consumers were stockpiling tissue products during the outbreak of the coronavirus in Q1 2020.

Profitability for both the tissue and personal care operations has been fairly stable over the last decade, which also indicates Essity's ability to manage its key input costs. Some of the input costs, such as pulp (36% of total raw materials and consumables, and around 15% of total operating expenses at the group level in 2021) and recycled paper (9.5% of total raw materials and consumables, and around 4% of total operating expenses), have fairly high volatility, and price increases can be typically passed on to customers only with delays of up to one year. Even in an environment of substantially increasing pulp prices in 2017 and H1 2018, the company delivered a fairly robust performance, with less volatility than that of its key tissue peers in Europe.

Exhibit 7

Essity has had fairly stable demand patterns and profitability through the cycle



Change in the reporting segments in 2017 with retrospective changes until 2015. The segment previously named tissue is now split into professional hygiene and consumer tissue. Data as reported by the company (that is, without Moody's adjustments).

Sources: Essity financial reports and former Svenska Cellulosa Aktiebolaget segmental reporting

M&A risk, but within the limits of Essity's financial policies, which target a solid investment-grade rating

Essity's financial policies are centred around its commitment to retain a solid investment-grade rating, which drives its capital allocation priorities, including dividend payouts, as well as M&A. Although the company will continue to complement organic growth with M&A in the next couple of years, especially in the area of medical devices with low technology content, where the market is still relatively fragmented, at this point, there is little capacity for debt-funded growth.

While Essity's leverage currently exceeds the upper end of the 2.0x - 3.0x range set for the Baa1 rating category we still consider the rating to be solidly positioned. We believe that Essity will be willing and able to operate with a leverage below 3.0x through the cycle, supported by both EBITDA growth, as the company continues to pass through high pulp prices to its customers, and actual debt repayments. Taking into consideration Essity's capital spending of 5%-6% of sales and dividends typically of around 50% of net income, we expect the company to continue to generate positive FCF in the high-single-digit to low-double-digit percentages of

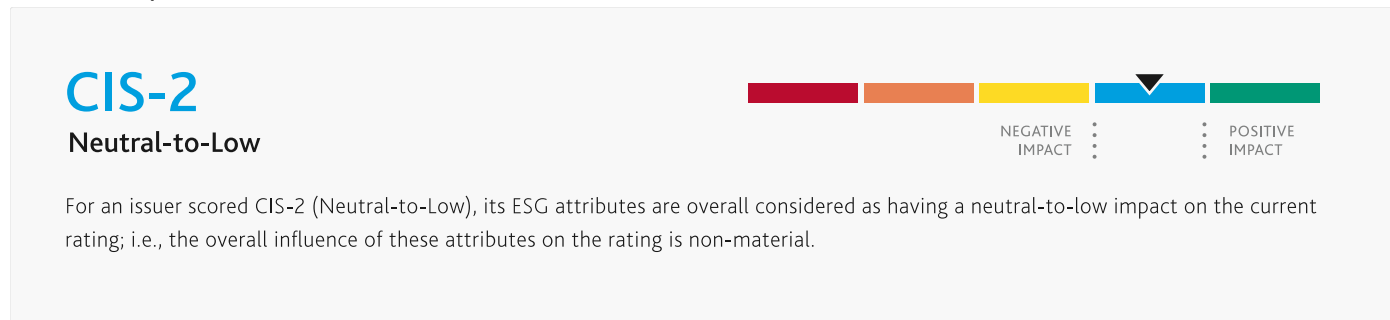
Moody's-adjusted gross debt, which could be potentially used for debt repayments. We will assess further smaller acquisitions within the limits of the company's FCF on a case-by-case basis.

ESG considerations

ESSITY AKTIEBOLAG's ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 8

ESG Credit Impact Score



Source: Moody's Investors Service

The neutral to low Credit Impact Score (**CIS-2**) given to Essity combines moderately negative scores for environmental and social risks and a neutral to low assessment for Governance risk supported by a strong sub-score for Financial strategy & Risk Management within governance.

Exhibit 9

ESG Issuer Profile Scores



Source: Moody's Investors Service

Environmental

Environmental risks are moderately negative. While Carbon transition, water management and physical climate risk are considered to be low to neutral Essity has a moderately negative exposure with regard to waste & pollution as well as to natural capital given the release of air pollutants and hazardous waste in line with industry peers and in view of the use of pulp in the production process.

Social

Social risks are moderately negative, driven by the industry-wide exposure to risks related to health & safety, responsible production and demographic and societal trends, while Essity has neutral to low risk related to customer relations and human capital.

Governance

Governance risks are neutral to low (**G-2**). Essity scores moderately negative on board structure and policies given it has A and B shares with different voting rights and a concentrated ownership. However, this is balanced by a strong score for financial strategy & risk management reflecting its conservative financial policy, aimed at protecting its solid investment-grade rating.

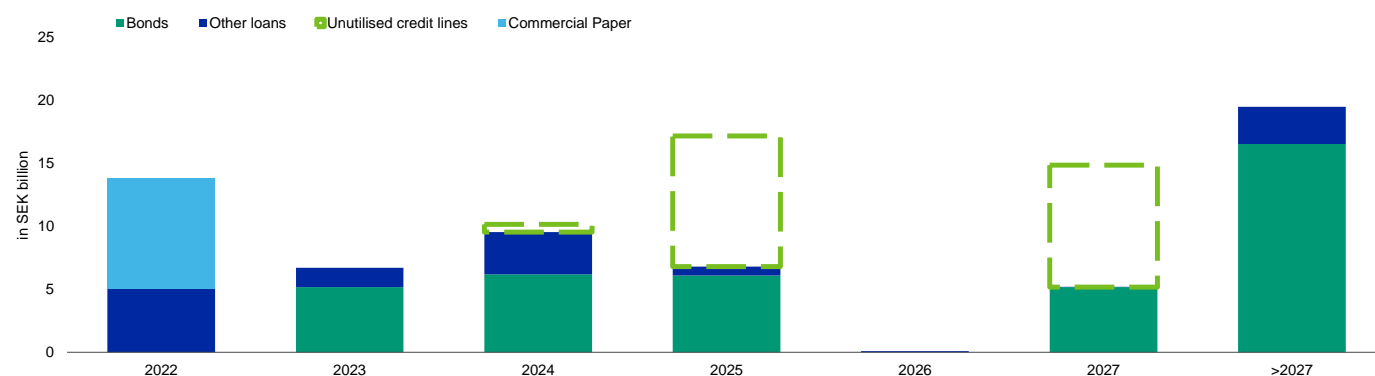
ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Liquidity analysis

We consider Essity's liquidity to be good, primarily based on our expectation that the company will continue to generate significant positive FCF over the next four to six quarters. As of the end of March 2022, the company reported around SEK5.3 billion of cash and cash equivalents, roughly one-third of those in countries with currency restrictions. In addition, the company has access to various largely undrawn credit facilities, totalling roughly SEK20 billion, consisting primarily of two syndicated facilities, each of around €1.0 billion, maturing in 2025 and 2027 respectively. The facilities are of high quality, without material adverse change clauses and other conditionality language, and have also served as backstop facilities for the company's commercial paper programme, which has been a central source of Essity's short-term funding needs. As of the end of March 2022, the company reported roughly SEK14.8 billion in short-term debt, which includes SEK8.8 billion under Essity's commercial paper program. The company's maturity profile is generally well spread, with an average maturity of around 4.6 years.

Exhibit 10

Essity's debt maturity profile is generally well spread As of 31 March 2022



Source: Essity reporting

Rating methodology and scorecard factors

The principal methodology used in rating Essity is Moody's Consumer Packaged Goods Methodology, published in February 2020. Adjusted for the timing of dividend payments the scorecard-indicated outcome indicates a Baa1 rating for the 12 months that ended March 2022, in line with the rating assigned.

Exhibit 11

Essity Aktiebolag

Consumer Packaged Goods Industry Scorecard [1][2]		Current LTM 3/31/2022 [3]		Moody's 12-18 Month Forward View As of 5/31/2022 [4]	
Factor 1 : Scale (20%)	Measure	Score	Measure	Score	Score
a) Revenue (USD Billion)	\$14.6	A	\$16.2	A	A
Factor 2 : Business Profile (30%)					
a) Geographic Diversification	A	A	A	A	A
b) Segmental Diversification	Baa	Baa	Baa	Baa	Baa
c) Market Position	A	A	A	A	A
d) Category Assessment	A	A	A	A	A
Factor 3 : Profitability (10%)					
a) EBITA Margin	10.0%	B	11.3%	B	B
Factor 4 : Leverage and Coverage (25%)					
a) Debt / EBITDA	3.5x	Ba	2.9x	Baa	Baa
b) RCF / Net Debt	9.3%	B	22.5%	Baa	Baa
c) EBITA / Interest Expense	13.6x	Aa	15x	Aa	Aa
Factor 5 : Financial Policy (15%)					
a) Financial Policy	A	A	A	A	A
Rating:					
a) Scorecard-Indicated Outcome		Baa2			Baa1
b) Actual Rating Assigned					Baa1

[1] All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

[2] As of FYE 12/31/2021.

[3] Adjusted for the timing of dividend payment we calculate leverage of 3.3x Debt / EBITDA and retained cash flow coverage of 18.1% RCF / Net Debt for the 12 months that ended March 2022.

[4] This represents Moody's forward view, not the view of the issuer, and does not incorporate significant acquisitions and divestitures.

Source: Moody's Financial Metrics™

Ratings

Exhibit 12

Category	Moody's Rating
ESSITY AKTIEBOLAG	
Outlook	Stable
Issuer Rating	Baa1
Senior Unsecured	Baa1
ST Issuer Rating	P-2

Source: Moody's Investors Service

Appendix

Exhibit 13

Peer comparison

(in USD million)	Essity Aktiebolag Baa1 Stable			Procter & Gamble Company (The) Aa3 Stable			Kimberly-Clark Corporation A2 Stable		
	FYE	FYE	LTM	FYE	FYE	LTM	FYE	FYE	LTM
	Dec-20	Dec-21	Mar-22	Jun-20	Jun-21	Mar-22	Dec-20	Dec-21	Mar-22
Revenue	13,265	14,213	14,622	70,950	76,118	79,618	19,140	19,440	19,792
EBITDA	2,654	2,333	2,198	19,874	21,536	21,318	4,613	3,827	3,752
Total Debt	6,125	6,560	7,300	44,246	40,469	42,150	9,096	9,190	9,920
Cash & Cash Equivalents	450	277	416	16,181	10,288	8,526	303	270	493
EBIT margin %	13.7%	10.4%	8.9%	23.4%	24.4%	23.0%	19.2%	15.0%	14.4%
EBIT / Interest Expense	14.2x	14.1x	12.0x	25.5x	29.1x	30.7x	13.2x	10.6x	10.3x
Debt / EBITDA	2.1x	3.0x	3.5x	2.2x	1.9x	2.0x	2.0x	2.4x	2.6x
RCF / Net Debt	29.6%	19.4%	9.3%	30.4%	32.5%	26.9%	24.3%	14.1%	11.5%
FFO / Debt	37.0%	27.6%	23.8%	36.9%	44.7%	42.1%	39.4%	30.2%	26.4%

All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

Source: Moody's Financial Metrics™

Exhibit 14

Reconciliation of debt

Essity Aktiebolag

(in SEK million)	FYE	FYE	FYE	FYE	FYE	LTM
	Dec-17	Dec-18	Dec-19	Dec-20	Dec-21	Mar-22
As Reported Total Debt	54,124	53,742	51,227	46,096	56,895	65,532
Pensions	3,622	3,830	4,133	4,207	2,500	2,500
Leases	2,328	3,334	0	0	0	0
Non-Standard Adjustments	(195)	(570)	(461)	0	0	0
Moody's Adjusted Total Debt	59,879	60,336	54,899	50,303	59,395	68,032

Source: Moody's Financial Metrics™

Exhibit 15

Reconciliation of EBITDA

Essity Aktiebolag

(in SEK million)	FYE	FYE	FYE	FYE	FYE	LTM
	Dec-17	Dec-18	Dec-19	Dec-20	Dec-21	Mar-22
As Reported EBITDA	18,036	17,500	21,941	24,517	20,689	20,023
Pensions	(14)	10	21	(155)	24	24
Leases	776	980	0	0	0	0
Unusual Items	230	20	160	0	(706)	(706)
Non-Standard Adjustments	(169)	(63)	(60)	0	0	0
Moody's Adjusted EBITDA	18,859	18,447	22,062	24,362	20,007	19,341

We define EBITDA as pretax income + gross interest expense + depreciation and amortisation.

Source: Moody's Financial Metrics™

Exhibit 16

Overview of key metrics

Essity Aktiebolag

(in SEK million)	FYE Dec-17	FYE Dec-18	FYE Dec-19	FYE Dec-20	FYE Dec-21	LTM Mar-22
INCOME STATEMENT						
Revenue	109,265	118,500	128,975	121,752	121,867	128,640
EBITDA	18,859	18,447	22,062	24,362	20,007	19,341
EBIT	12,435	11,442	14,585	16,691	12,616	11,420
Interest Expense	1,472	1,517	1,540	1,179	896	949
BALANCE SHEET						
Cash & Cash Equivalents	3,209	1,866	2,236	3,699	2,508	3,877
Total Debt	59,879	60,336	54,899	50,303	59,395	68,032
Net Debt	56,670	58,470	52,663	46,604	56,887	64,155
CASH FLOW						
Funds from Operations (FFO)	14,284	16,148	15,937	18,617	16,365	16,177
Capital Expenditures	(6,819)	(7,712)	(6,746)	(7,504)	(8,202)	(8,382)
Dividends	285	4,435	4,374	4,813	5,312	10,185
Retained Cash Flow (RCF)	13,999	11,713	11,563	13,804	11,053	5,992
RCF / Net Debt	24.7%	20.0%	22.0%	29.6%	19.4%	9.3%
Free Cash Flow (FCF)	6,284	1,819	8,192	5,483	1,102	(3,374)
FCF / Debt	10.5%	3.0%	14.9%	10.9%	1.9%	-5.0%
PROFITABILITY						
% Change in Sales (YoY)	7.9%	8.5%	8.8%	-5.6%	0.1%	11.3%
EBIT margin %	11.4%	9.7%	11.3%	13.7%	10.4%	8.9%
EBITDA margin %	17.3%	15.6%	17.1%	20.0%	16.4%	15.0%
INTEREST COVERAGE						
EBIT / Interest Expense	8.4x	7.5x	9.5x	14.2x	14.1x	12.0x
EBITDA / Interest Expense	12.8x	12.2x	14.3x	20.7x	22.3x	20.4x
(EBITDA - CAPEX) / Interest Expense	8.2x	7.1x	9.9x	14.3x	13.2x	11.5x
LEVERAGE						
Debt / EBITDA	3.2x	3.3x	2.5x	2.1x	3.0x	3.5x
Debt / (EBITDA - CAPEX)	5.0x	5.6x	3.6x	3.0x	5.0x	6.2x
Net Debt / EBITDA	3.0x	3.2x	2.4x	1.9x	2.8x	3.3x

All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

Source: Moody's Financial Metrics™

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