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CREDIT OPINION
5 January 2018

Update

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RATINGS

Essity Aktiebolag

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

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.

Contacts

Martin Fujerik +49.69.7073.0909
VP-Senior Analyst
martin.fujerik@moodys.com

Karoline Metzger +49.69.7073.0912
Associate Analyst
karoline.metzger@moodys.com

Matthias Hellstern +49.69.7073.0745
MD-Corporate Finance
matthias.hellstern@moodys.com

Essity Aktiebolag

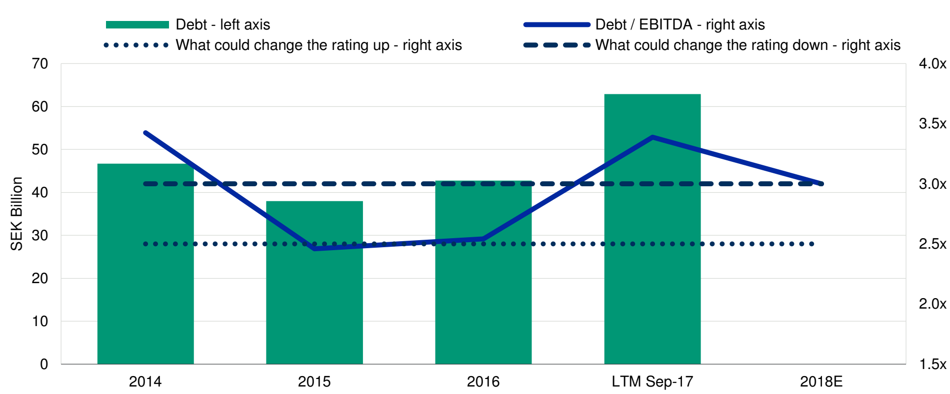
Update of the analysis of key credit factors

Summary

The Baa1/P-2 ratings for Essity Aktiebolag (Essity) primarily recognise (1) its sizable scale, with revenue of SEK107 billion for the 12 months ended September 2017 (around US$12 billion); (2) its leading market positions across the portfolio in countries where it operates, with both branded and private-label products; (3) its global footprint, with emerging markets representing one third of revenue; (4) fairly good underlying growth and stability of demand for its products; and (5) its financial policies aimed at protecting its solid investment-grade rating.

Essity's ratings are primarily constrained by (1) the company's exposure to fairly volatile input prices, such as pulp and recycled paper; (2) the somewhat below-average profitability compared with most of its similarly rated peers, with a Moody's-adjusted EBIT margin of around 11% in 2016; (3) some debt-funded M&A risk, yet within the company's financial-policy commitment to maintaining a solid investment-grade rating. Following the debt-funded acquisition of BSN Medical in April 2017 for a purchase price of around €2.7 billion, Essity's leverage continues to be elevated (Moody's-adjusted debt/EBITDA estimated at around 3.4x for the 12 months ended September 2017) and positions Essity weakly in the Baa1 rating, as indicated by a negative outlook. Even if negative pressure on the ratings eased through 2017, the maintenance of a Baa1 rating would require further sustainable deleveraging through 2018.

Exhibit 1
Following the acquisition of BSN Medical, Essity's leverage will continue to be elevated, at least through 2018



All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Forward view represents Moody's view and does not incorporate any material divestments and acquisitions (other that the acquisition of BSN Medical).
Source: Moody's Financial Metrics

Credit strengths

» Strong business profile with a broad portfolio of well positioned global (Tork, Tena) and regional brands

» Fairly good underlying growth and stability of demand for the majority of the products

» Financial policy aimed at protecting its solid investment-grade rating

Credit challenges

» Exposure to volatile input costs such as pulp and recycled paper

» Ongoing need for innovation in the personal care and tissue business areas to preserve pricing levels

» Exposure to event risk such as potential M&A activity, alternatively shareholder returns and special dividend

Rating outlook

The negative outlook reflects weak positioning at the Baa1 level following the fully debt-financed acquisition of BSN and the still relatively elevated risk that Essity will not be able to deleverage to 3.0x by the end of 2018.

Factors that could lead to an upgrade

» EBIT margins consistently above 12% throughout all business areas

» RCF/net debt clearly above 25%

» Debt/EBITDA well below 2.5x

» Continued positive free cash flow generation applied towards debt reduction

Factors that could lead to a downgrade

» A decline in the EBIT margin to below 9%

» RCF/net debt falling sustainably below 20%

» Debt/EBITDA deteriorating towards 3x

» Free cash flow turning negative

» Erosion of the company's solid liquidity profile

Key indicators

Exhibit 2
Key Indicators for Essity

	12/31/2014	12/31/2015	12/31/2016	09/30/2017 (LTM) [1]	next 12-18 months
Total Sales (USD Billion)	$12.9	$11.7	$11.8	$12.0	$12.0 - $13.0
EBIT Margin	9.9%	10.2%	10.9%	11.5%	11.5% - 13.0%
Debt / EBITDA	3.4x	2.5x	2.5x	3.4x	2.7x - 3.2x
RCF / Net Debt	24.5%	35.9%	28.0%	20.9%	20% - 25%
EBIT / Interest Expense	6.9x	8.1x	8.9x	8.2x	8.5x - 9.5x

[1] Moody's estimates with roughly two quarters of BSN Medical results consolidated.
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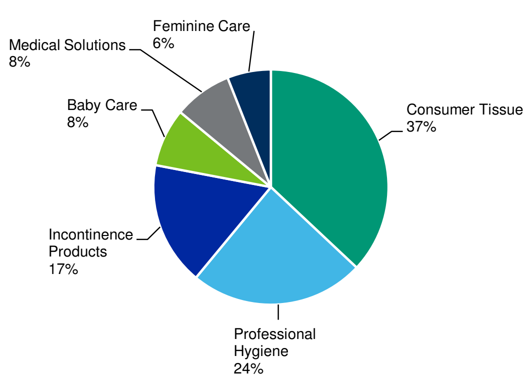
Source: Moody's Financial Metrics

Profile

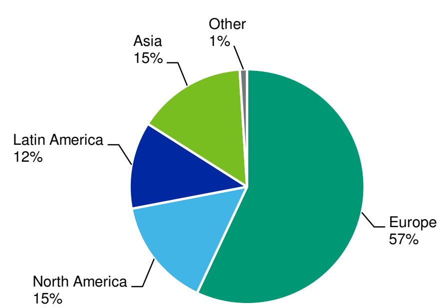
Headquartered in Stockholm, Sweden, Essity is one of the leading global hygiene and health companies, with sales of SEK107 billion for the 12 months ended September 2017 (around US$12 billion). The company develops, produces and sells a wide range of products, including incontinence products, baby diapers, feminine-care products, consumer tissue, away-from-home (AfH) tissue, and products for wound care, compression therapy and orthopedics. With a workforce of roughly 50,000 employees, Essity operates in about 150 countries worldwide under a number of well-recognised brands. Essity was formed in 2016 as a spin-off of the tissue and personal care operations of Svenska Cellulosa Aktienbolaget SCA. The company is listed on the Stockholm stock exchange with a market capitsalisation of around SEK170 billion as of 12 December 2017.

Exhibit 3
Revenue split by product
Third quarter of 2017



Source: Essity reports

Exhibit 4
Revenue split by geography
2016 revenue



Source: Essity's annual report

Detailed Credit Considerations

Wide portfolio with a number of leading positions globally

Essity's Baa1/P-2 ratings recognise that, with sales of over SEK100 billion, Essity is one of the leading global hygiene and health companies, active in around 150 countries. 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, Essity has strong brands and market positions within the markets for baby diapers, feminine care, consumer tissue, as well as regional and global brands and leading market positions in wound care, compression therapy and orthopedics with brands such as Jobst and Leukoplast. Overall, Essity 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 Diapers	#4	#2	-	#6	#6	Drypers, Pequenín, Libero
Feminime Care	#6	#3	-	#1	#12	Libresse, Saba, Nosotras, Bodyform
Medical Devices	#4	n.a.	n.a.	n.a.	n.a.	Leuko, Cutimed, Jobst, Delta, Actimove
Consumer Tissuer	#2	#1	-	#3	#1	Tempo, Edet, Zewa, Lotus, Plenty, Vinda
Professional Hygiene	#1	#1	#2	#3	#3	Tork

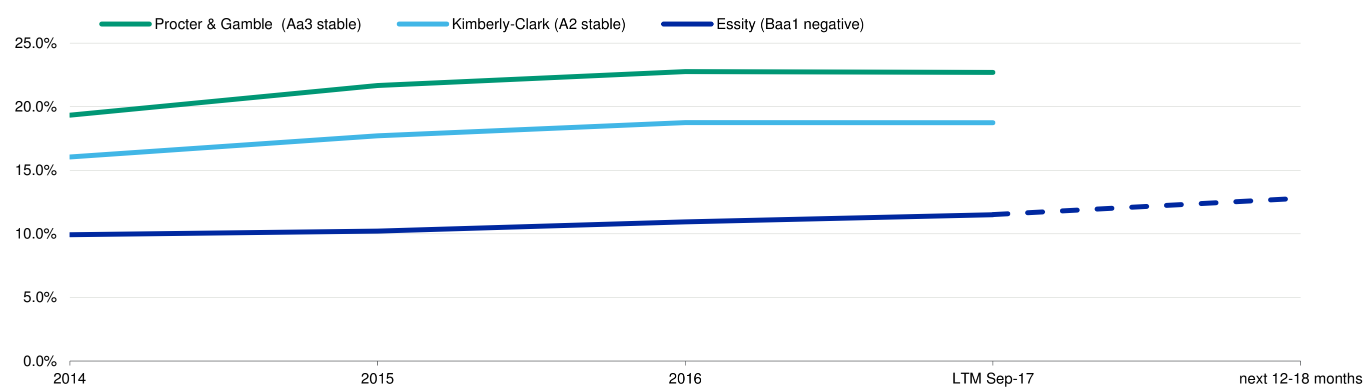
Source: Essity annual reports

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, as well as optimise costs. In the tissue business, which is generally more competitive and less profitable, Essity competes primarily with Georgia-Pacific (G-P, A3, stable), Hengan, Kimberly-Clark (K-C, A2 stable) and Sofidel. In the personal care business Essity's key competitors are K-C, Procter & Gamble (P&G, Aa3 stable) and Unicharm. In April 2017, following the debt-funded acquisition of BSN Medical for a purchase price of €2.7 billion, Essity entered the market for medical devices with low technology content, which benefits from robust and stable demand and above-average profitability.

We expect Essity to focus on growing its personal care and the medical devices product offerings, while further increasing the efficiency of the tissue operations. This strategy will help narrow the profitability gap with Essity's more profitable competitors, especially K-C and P&G, which benefit from a higher share of the more profitable personal care business and higher share of the generally more profitable US market.

Exhibit 6

Essity's margins have been below that of its main competitors, but we expect the gap to narrow somewhat
Moody's-adjusted EBIT margin



All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
Forward view represents Moody's view; not the view of the issuer.
Source: Moody's Financial Metrics

Good underlying demand growth, especially in emerging markets

Essity benefits from the fact that demand for its products enjoys good underlying growth, 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 experience modest annual growth in low single digits in percentage terms, the growth potential in emerging markets is substantial and we estimate the annual growth rate there in high single digits in percentage terms. This is because per capita consumption of tissue and personal care products in emerging markets is significantly lower in an environment where living standards are rapidly improving.

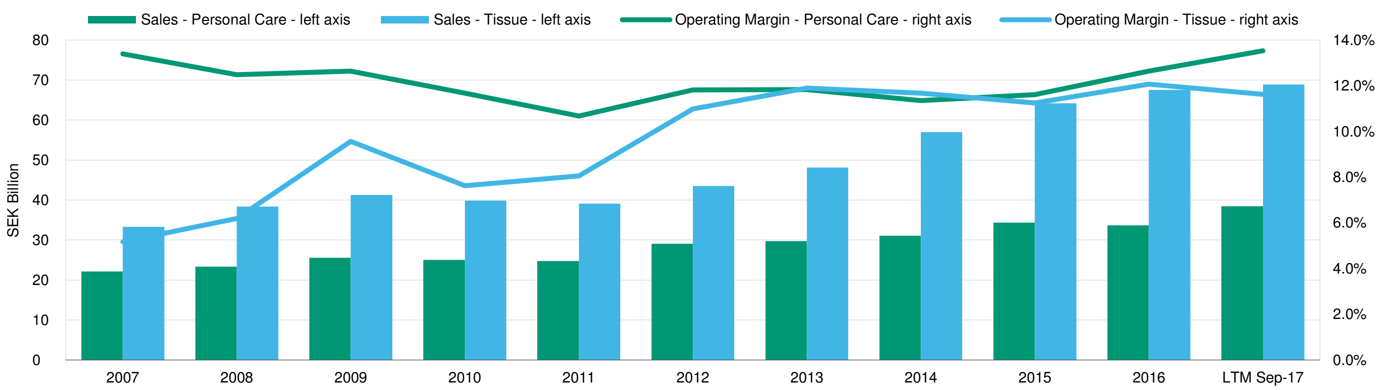
To benefit from this development, Essity has focused on growing its presence in emerging markets over the past decade. This was done both organically, as well as through M&A, most recently through an acquisition of a majority stake in Hong-Kong-based tissue company Vinda in 2014. Currently, emerging markets represent roughly one third of revenue and we expect this share to increase further.

Stable underlying demand, but exposure to volatile input costs

Demand for Essity products has historically exhibited fairly good stability through the cycle. Even in the 2008-09 global economic downturn, which was unprecedented in its magnitude, Essity hardly faced any organic decline in sales, and margins for both the tissue and personal care businesses remained robust. The 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 them, such as pulp (16% of total operating expenses at the group level in 2016) and recycled paper (4%), exhibit fairly high volatility and price increases can be typically passed to customers only with delays up to one year.

Exhibit 7

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



Operating Margin is as reports by the company

Sources: Essity reports and former Svenska Cellulosa Aktiebolaget segmental reporting

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

Essity's financial policies are centered around its commitment to retain a solid investment-grade rating, which drives its capital allocation priorities, including dividend payouts, as well as M&A. Even though we believe that in the medium term Essity will continue to complement organic growth with M&A, especially in the area of medical devices with low technology content where the market is still relatively fragmented, at this point there is limited capacity for debt-funded growth.

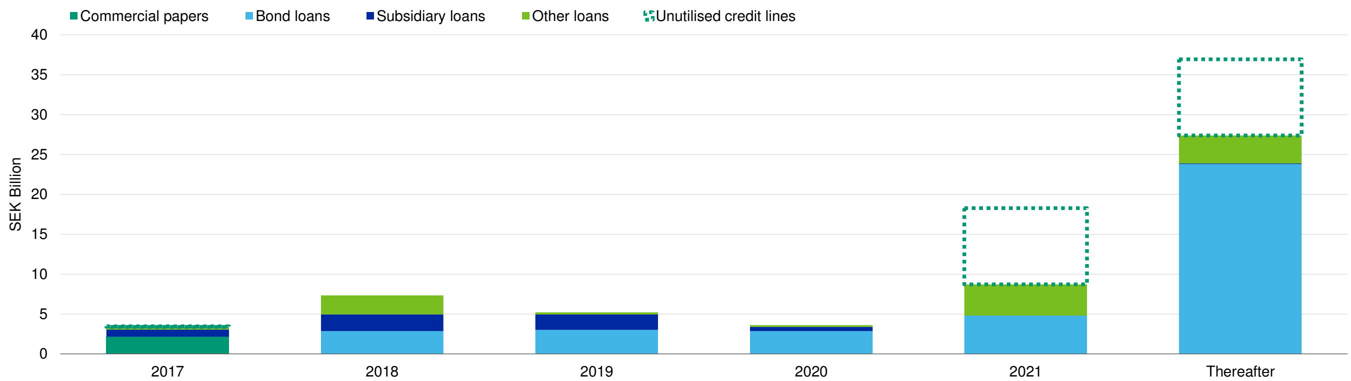
Following the acquisition of BSN Medical in April 2017, Essity's leverage continues to be elevated (Moody's-adjusted debt/EBITDA estimated at around 3.4x for the 12 months ended September 2017) and positions Essity weakly in the Baa1 rating category. Even if negative pressure on the ratings eased through 2017, the maintenance of a Baa1 rating requires further sustainable deleveraging through 2018. Considering capital spending of around 5%-6% of sales and dividends typically of around 50% of net income, we expect Essity to continue generating positive free cash flow (FCF) in high single digits in percentage terms of Moody's-adjusted gross debt, which could be used for debt repayments. We will consider further smaller acquisitions within the limits of Essity's FCF generation on a case-by-case basis.

Liquidity analysis

We consider Essity's liquidity profile to be good, primarily based on our expectation of Essity continuing to generate meaningful positive FCF over the next six quarters. As of the end of September 2017, the company reported around SEK4.4 billion of cash and cash equivalents, roughly one third of which were in countries with currency restrictions. In addition, Essity has access to various largely undrawn credit facilities totaling roughly SEK19.2 billion, primarily consisting of two syndicated facilities, each €1.0 billion, maturing in 2019 and 2021. In December 2017 Essity signed a new €1.0 billion facility, replacing the 2019 maturity, with maturity in 2023 and with two extension options of one year each. The facility becomes effective in January 2019.

The facilities are of high quality, without material adverse change clauses and other conditionality language and have also served as backstop facilities for the commercial paper programme, which has been a central source of Essity's short-term funding needs. As of the end of September 2017, Essity reported roughly SEK6.2 billion of short-term debt, which includes around SEK2.2 billion of issued commercial papers. Essity's maturity profile is well spread, with an average maturity of 4.3 years.

Exhibit 8
Essity's debt maturity profile is well spread
As of third quarter 2017



The credit facility with the marked maturity in 2023 will replace equally sized facility maturing in 2019
Source: Essity reports

Rating methodology and scorecard factors

The principal methodology used in rating Essity is the Global Packaged Goods Rating Methodology. The methodology grid indicates a weak A3 rating for 2016 credit metrics, as well as for our 12-18 month forward-looking view, which already incorporates the acquisition of BSN Medical. The one notch difference is mainly attributed to a weak positioning of Essity in the A category for the Geographic Diversification, Category Assessment and Financial Policy sub-factors.

Exhibit 9
Methodology grid for Essity

Consumer Packaged Goods Industry Grid	Current FY 12/31/2016		Moody's 12-18 Month Forward View As of 12/13/2017	
Factor 1 : Scale and Diversification (44%)	**Measure**	**Score**	**Measure**	**Score**
a) Total Sales (USD Billion)	$11.8	A	$12.0 - $13.0	A
b) Geographic Diversification	A	A	A	A
c) Segmental Diversification	Baa	Baa	Baa	Baa
Factor 2 : Franchise Strength and Potential (14%)				
a) Market Share	A	A	A	A
b) Category Assessment	A	A	A	A
Factor 3 : Profitability (7%)				
a) EBIT Margin	10.9%	Ba	11.5% - 13%	Ba
Factor 4 : Financial Policy (14%)				
a) Financial Policy	A	A	A	A
Factor 5 : Leverage and Coverage (21%)				
a) Debt / EBITDA	2.5x	Baa	2.7x - 3.2x	Baa
b) RCF / Net Debt	28.0%	Baa	20% - 25%	Baa
c) EBIT / Interest Expense	8.9x	A	8.5x - 9.5x	A
Rating:				
a) Indicated Rating from Grid		A3		A3
b) Actual Rating Assigned				Baa1

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Source: Moody's Financial Metrics

Ratings

Exhibit 10

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

Source: Moody's Investors Service

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