

Sappi results for third financial quarter ended June 2019

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Financial summary for the quarter

- EBITDA excluding special items US\$118m (Q3 2018 US\$155m)
- Profit for the period US\$8m (Q3 2018 US\$51m)
- EPS excluding special items 4 US cents (Q3 2018 10 US cents)
- Net debt US\$1,728m (Q3 2018 US\$1,603m)

Commenting on the result, Sappi Chief Executive Officer Steve Binnie said: “Although our 3rd quarter is traditionally lower due to northern hemisphere summer holidays, the results for the quarter were under pressure. We faced challenging market conditions across all our major product categories, but in particular from sluggish graphic paper demand in Europe and North America which necessitated production downtime and weak dissolving wood pulp (DWP) prices due to soft viscose staple fibre (VSF) markets. In addition, annual maintenance shuts which impact production and sales volumes were completed at Ngodwana, Saiccor and Cloquet mills.”

“Notwithstanding a tough quarter, we continued to focus on executing our strategy to diversify our product portfolio into higher margin segments to position us for future growth. The recent projects to increase capacity at each of our DWP mills and convert capacity at Somerset and Maastricht mills towards packaging boosted sales volumes in each of these segments during the quarter, thereby lessening the impact of particularly weak graphic paper markets.”

The group earnings excluding special items decreased from US\$155m to US\$118m, with profit for the period decreasing from US\$51m to US\$8m due to lower operating profit and a US\$9m once-off finance cost charge for the refinancing of the 2022 bonds.

VSF markets were under significant pressure due to excess capacity and weak textile exports from China. This impacted VSF producer margins and together with low paper pulp prices reduced DWP prices to their lowest level in a decade.

Packaging and specialities markets were mixed across our regions, with demand for packaging offsetting weakness in the consumer speciality grades. The ramp up of commercial volumes from both Somerset and Maastricht proceeded according to plan, although profitability was constrained by the product qualification process as well as lower average selling pricing during the period.

In Europe Sappi gained significant market share in coated woodfree paper as competitors looked to exit the market. Higher average net selling prices and purchased pulp prices that declined throughout the quarter partially offset the impact of weak graphic paper sales into the publishing sector in Europe. Volumes in the packaging and specialities business were flat with stable packaging demand offsetting weakness in consumer speciality products. The conversion of Lanaken PM8 from coated mechanical to coated woodfree was completed during the quarter.

The North American business remained under pressure. Weak graphic paper markets, lower dissolving wood pulp prices, the annual maintenance shut at Cloquet mill and the continued ramp-up for Somerset PM1 all weighed on margins. Commercial sales volumes for Somerset PM1 paperboard grades were up 38% on the prior quarter and overall packaging and speciality volumes were 88% higher than the prior year.

The Southern African results were impacted by lower average US\$ pricing for DWP and a delayed start to the citrus season which impacted containerboard sales volumes.

Looking towards the rest of the year, Binnie indicated that “Given the current weak market conditions for graphic paper, DWP pricing pressure from oversupplied VSF markets and global economic uncertainty related to trade wars, our fourth quarter profitability will likely be below that of the prior year.”

Outlook

DWP pricing is expected to continue to be under pressure whilst VSF producers are impacted by low margins, paper pulp prices remain low and uncertainty exists in textile markets as a result of the US/China trade tensions. Sappi's DWP sales volumes are expected to stay healthy and the expanded production capacity at Saiccor, Ngodwana and Cloquet will be utilised to meet customer demand.

Packaging and specialities markets show good growth prospects; however, growth has slowed in some segments due to general economic conditions. Raw material prices, particularly paper pulp, are declining and offer some relief for margins. Demand for South African packaging products is expected to be strong going into the local spring. The ramp-up and product mix optimisation process continues at Somerset and Maastricht as qualification and customer acceptance is completed. As mentioned in the results announcement, the acquisition of Matane mill will increase the pulp integration for our North American and European packaging businesses, and lower costs going forward.

Persistent weakness in graphic paper markets will require further production downtime in the coming quarter. Sufficient capacity is expected to be shut or converted within the industry, thereby allowing operating rates and margins to recover in future periods. Lower paper pulp prices are offering some relief, however paper prices in both US and Europe have declined due to current market conditions.

Capital expenditure for the remainder of the year is expected to be approximately US\$200m as Sappi continue the transition to growing and higher margin segments. Major projects currently underway include the 110,000t expansion at Saiccor mill and the final commissioning of Lanaken PM8 after the conversion from coated mechanical to coated woodfree paper. No other major projects are currently committed and therefore we expect annual capex levels to reduce over the next two years.

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Sappi



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