

# Essity AB

December 20, 2024

**Essity's expanding EBITDA margin and healthy free operating cashflow should translate in S&P Global Ratings-adjusted debt to EBITDA falling to about 1.5x in 2024, from 2.3x in 2023.**

In the first nine months of 2024, Essity's reported EBITDA stood at Swedish krona (SEK) 19.7 billion, compared with SEK18.8 billion in the previous year, resulting in an EBITDA margin of 18.2%, up by almost 400 basis points year-on-year. This is primarily attributable to the group's improvements in its product mix across the different divisions. We note the group concluded the restructuring of the professional hygiene division (about 26% of total revenues as of Sept. 30, 2024), exited low-profitability contracts for incontinence products in healthcare, and is reducing its exposure to the more volatile tissue business (accounting 31% of total revenues as of Sept. 30, 2024 down from 40% in 2021). We also believe the group's EBITDA benefits from the disposal of its 51.6% stake in Hong Kong-listed personal hygiene company Vinda International Holdings Ltd, which concluded in March 2024, as the sale of the group's stake in Vinda also reduces Essity's exposure to pulp. In terms of topline, for 2024, we anticipate sales to decline moderately by 2.0%-2.5%, on the back of 1.0%-1.5% reduction of sales prices compared to previous year and adverse foreign exchange movements. That said, we expect the group's S&P Global Ratings-adjusted EBITDA margin to rise to 17.5%-18% in 2024, from 16.1% at year-end 2023. We also forecast Essity to generate healthy free operating cash flow (FOCF) of SEK10 billion-SEK11 billion in 2024, broadly in line with 2023 but significantly up from SEK6 billion posted in 2022.

**Credit metrics remain well placed for the 'BBB+' rating--we factor in potential acquisitions and discretionary spending which could result in a leverage uptick from current levels.** We do not assume the group will consistently keep its leverage at or below 1.5x, and we expect it to return to about 2x in the medium term, commensurate with the current 'BBB+' rating and with Essity's commitment to a solid investment grade rating. We believe in 2024 Essity has increased its financial flexibility following the sale of its shareholding in Vinda, which resulted in a cash inflow of approximately SEK19 billion. On top of the commitment to pay long-term stable and rising annual cash dividends, in June 2024, the group launched a SEK3 billion share-buyback program, running until March 2025. We understand share buybacks will remain a recurring part of Essity's capital allocation policy, therefore we do not rule out the possibility of further buybacks from 2025, within the limits of maximum 10% of the total shares outstanding (641.9 million class B shares as of Dec. 16, 2024). We also believe Essity will continue looking at M&A opportunities, which remain part of its capital allocation policy. The group will focus on value accretive transactions that could either expand its product offering or add new production capabilities the company currently does not have.

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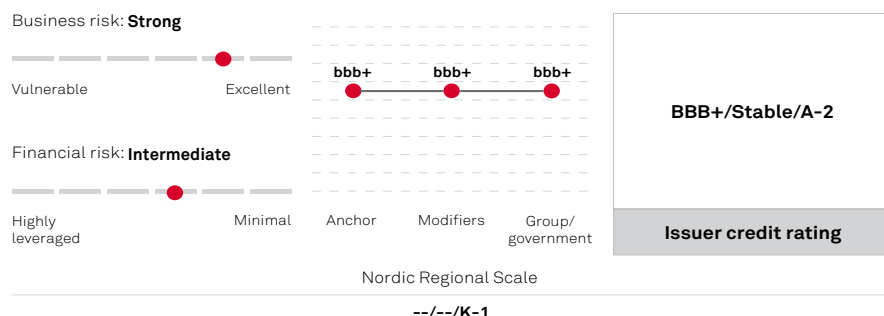
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**Uncertainty remains around the potential early repayment of Essity’s notes, although in our view the group is prudently handling liquidity risk.**

In October 2024, few bondholders demanded for early repayment of a minority part of Essity’s bonds maturing in 2029, 2030, and 2031, claiming that following the disposal of the stake in Vinda, an event of default occurred on the group’s medium-term loan (MTN) program, with a total outstanding amount of SEK35.7 billion (the total size is €6 billion). On Dec. 16, 2024, the company announced that some of these bondholders, whose holdings represented a small portion of the outstanding bonds, have initiated proceedings in an English court. The company continues to reject the claims of a right to early repayment under the terms of its bonds and considers the demand to be unfunded. We do not have visibility on the possible outcome and on timing of the court ruling, although we recognize the group signed committed credit facilities in order to offset any potential liquidity pressure coming from the bondholders’ demand. As of Sept. 30, 2024, the group had about SEK81.8 billion (€7.1 billion) total available liquidity, comprising of SEK67.6 billion (about €6 billion) committed credit facilities maturing beyond 12 months and about SEK11.8 billion (about €1 billion) in cash and cash equivalents.

## Ratings Score Snapshot



## Recent Research

- Industry Credit Outlook Update Europe: Consumer Products, July 18, 2024
- Bulletin: Essity's New Committed Credit Facility Supports Its Liquidity Profile, March 11, 2024
- Bulletin: Essity's Agreement To Sell Its Vinda Stake Enhances Financial Flexibility, Dec. 15, 2023

## Company Description

Essity is a Swedish health and hygiene group that was created when Svenska Cellulosa spun off its hygiene division in 2017. Essity produces and sells personal care, tissue, and health and medical products. In the 9 months ended Sept. 30, 2024, Essity posted roughly SEK108 billion in sales (down about 2.5% versus the same period a year earlier) and reported EBITDA of about SEK19.7 billion, with an EBITDA margin of 18.2%.

Essity operates through three main divisions:

- Consumer goods (54% of Essity’s sales as of September 2024). This division sells adult incontinence products retail (global market leadership with the TENA brand), baby care

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products (such as baby diapers and pants), feminine care products (pads, panty liners, and tampons), and consumer tissue products (toilet paper, household towels, facial tissues, wet wipes, napkins, and face masks), via the retail trade channel and online.

- Professional hygiene (26% of sales). This division develops and markets complete hygiene solutions under the leading global brand TORK. These include toilet paper, paper hand towels, napkins, hand sanitizer, tissues, and dispensers. The division also provides services and maintenance for companies and office buildings, universities, health care facilities, restaurants, hotels, and other public venues.
- Health and medical (20% of sales). Comprising incontinence products health care and medical solutions (wound care, compression therapy, and orthopedics products). Essity has established a solid presence in this market following its acquisition of BSN in 2017. Its global and regional brands include Tena, Leukoplast and Jobst, among others.

Essity is present in more than 150 countries globally, with Europe accounting for 60% of total sales as of Dec. 31, 2023, Latin America 17%, North America 17%, and Asia 2%. Other countries account for the remaining 4%. Essity is listed on the Nasdaq Stockholm exchange, with its largest shareholder being AB Industrivärden, with about a 10.5% stake on Sept. 30, 2024. As of Dec. 20, 2024, Essity has a market capitalization of about \$18.7 billion.

## Outlook

The stable outlook reflects our view that Essity's established brand portfolio and product innovation will continue to support sales this year. S&P Global Ratings adjusted EBITDA margins should expand to 17.5%-18.0% this year from 16.1% in 2022, thanks to less challenging input cost conditions, mainly for pulp, and a more efficient supply chain. Since we do not expect significant acquisitions this year, we believe adjusted debt to EBITDA should reduce close to 1.5x in 2024 from 2.3x in 2023.

### Downside scenario

We could consider lowering the rating if we see consumers becoming a lot more price sensitive and shift to private-label products, causing Essity to lose market share or adopt high promotions that depress profitability. In this scenario, we would expect Essity's market position and operating performance to deteriorate, translating into adjusted debt to EBITDA staying higher than 3.0x.

We could also consider a negative rating action if we were to observe Essity adopting an aggressive financial policy, leading to large debt-funded acquisitions or unexpectedly large shareholder distributions, pushing debt to EBITDA above 3.0x for a prolonged period.

### Upside scenario

We could consider a positive rating action if Essity generated solid FOCF across its three divisions and used it to improve its leverage ratios, with debt to EBITDA approaching 2.0x. Under this scenario, the group would need to size its debt-funded acquisitions to ensure that it can maintain leverage at this level.

## Key Metrics

## Essity AB

### Essity AB--Key Metrics\*

Mil. SEK	2022a	2023a	2024e	2025f	2026f
Revenue	156,173	147,147	144,000-145,000	145,500-146,500	147,500-148,500
Revenue growth (%)	28.2	-5.8	(2.5)-(2.0)	1.0-1.5	1.0-1.5
EBITDA	20,112	23,760	25,000-26,000	25,500-26,500	26,000-27,000
EBITDA margin (%)	12.9	16.1	17.5-18.0	17.5-18.0	17.5-18.0
Funds from operations (FFO)	16,824	17,684	19,000-19,500	20,000-20,500	20,000-20,500
Capital expenditure	6,872	6,834	6,500-7,000	7,000-7,500	7,500-8,000
Free operating cash flow (FOCF)	5,340	12,269	10,000-11,000	10,000-11,000	10,500-11,500
Dividends	5,312	5,094	5,000-5,500	5,500-6,000	6,000-6,500
Debt	65,708	54,838	36,000-37,000	45,500-46,000	56,000-56,500
Debt to EBITDA (x)	3.3	2.3	Circa 1.5	Around 2	Around 2
FFO to debt (%)	25.6	32.2	53.0-54.0	43.5-44.5	35.5-36.5
FOCF to debt (%)	8.1	22.4	28.0-29.0	23.0-24.0	20.0-21.0
EBITDA interest coverage (x)	20.2	15.8	13.0-14.0	19.0-20.0	15.5-16.5
FFO interest coverage (x)	20.5	8.2	11.0-12.0	16.0-17.0	13.5-14.5

\*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate. f--Forecast.

## Financial Summary

### Essity AB--Financial Summary

Period ending	Dec-31-2018	Dec-31-2019	Dec-31-2020	Dec-31-2021	Dec-31-2022	Dec-31-2023
Reporting period	2018a	2019a	2020a	2021a	2022a	2023a
Display currency (mil.)	SEK	SEK	SEK	SEK	SEK	SEK
Revenues	118,500	128,975	121,752	121,867	156,173	147,147
EBITDA	18,266	21,973	24,120	19,958	20,112	23,760
Funds from operations (FFO)	14,760	19,755	19,311	15,486	16,824	17,684
Interest expense	1,117	1,126	912	815	997	1,503
Cash interest paid	1,040	1,088	892	838	862	2,461
Operating cash flow (OCF)	13,698	18,337	17,756	14,389	12,212	19,104
Capital expenditure	6,882	5,811	6,544	7,263	6,872	6,835
Free operating cash flow (FOCF)	6,816	12,526	11,212	7,126	5,340	12,269
Discretionary cash flow (DCF)	2,381	8,152	6,399	1,814	28	7,175
Cash and short-term investments	3,008	2,928	4,982	3,904	4,288	5,159
Gross available cash	3,008	2,928	4,982	3,904	4,288	5,159
Debt	57,147	51,769	44,011	54,931	66,554	55,756
Common equity	54,899	62,801	63,342	68,507	76,564	79,405
<b>Adjusted ratios</b>						
EBITDA margin (%)	15.4	17.0	19.8	16.4	12.9	16.1
Return on capital (%)	10.7	12.9	15.2	11.2	8.9	12.3
EBITDA interest coverage (x)	16.4	19.5	26.4	24.5	20.2	15.8
FFO cash interest coverage (x)	15.2	19.2	22.6	19.5	20.5	8.2

## Essity AB--Financial Summary

Debt/EBITDA (x)	3.1	2.4	1.8	2.8	3.3	2.3
FFO/debt (%)	25.8	38.2	43.9	28.2	25.3	31.7
OCF/debt (%)	24.0	35.4	40.3	26.2	18.3	34.3
FOCF/debt (%)	11.9	24.2	25.5	13.0	8.0	22.0
DCF/debt (%)	4.2	15.7	14.5	3.3	0.0	12.9

## Peer Comparison

## Essity AB--Peer Comparisons

	Essity AB	Kimberly-Clark Corp.	Henkel AG & Co. KGaA	Procter & Gamble Co.
Foreign currency issuer credit rating	BBB+/Stable/A-2	A/Stable/A-1	A/Stable/A-1	AA-/Stable/A-1+
Local currency issuer credit rating	BBB+/Stable/A-2	A/Stable/A-1	A/Stable/A-1	AA-/Stable/A-1+
Period	Annual	Annual	Annual	Annual
Period ending	2023-12-31	2023-12-31	2023-12-31	2024-06-30
Mil.	SEK	SEK	SEK	SEK
Revenue	147,147	205,462	239,144	890,715
EBITDA	23,760	41,593	35,115	247,387
Funds from operations (FFO)	17,684	32,094	28,379	191,427
Interest	1,503	3,375	1,078	10,216
Cash interest paid	2,461	2,983	1,123	9,717
Operating cash flow (OCF)	19,104	36,060	37,234	182,927
Capital expenditure	6,835	7,703	6,758	35,209
Free operating cash flow (FOCF)	12,269	28,357	30,476	147,718
Discretionary cash flow (DCF)	7,175	8,817	19,605	(4,036)
Cash and short-term investments	5,159	12,691	21,687	100,498
Gross available cash	5,159	12,691	24,143	100,498
Debt	55,756	78,819	10,227	298,891
Equity	79,405	10,740	222,304	535,866
EBITDA margin (%)	16.1	20.2	14.7	27.8
Return on capital (%)	12.3	35.0	10.6	26.1
EBITDA interest coverage (x)	15.8	12.3	32.6	24.2
FFO cash interest coverage (x)	8.2	11.8	26.3	20.7
Debt/EBITDA (x)	2.3	1.9	0.3	1.2
FFO/debt (%)	31.7	40.7	277.5	64.0
OCF/debt (%)	34.3	45.8	364.1	61.2
FOCF/debt (%)	22.0	36.0	298.0	49.4
DCF/debt (%)	12.9	11.2	191.7	(1.4)

**Rating Component Scores**

<b>Foreign currency issuer credit rating</b>	<b>BBB+/Stable/A-2</b>
<b>Local currency issuer credit rating</b>	<b>BBB+/Stable/A-2</b>
<b>Business risk</b>	<b>Strong</b>
Country risk	Low
Industry risk	Low
Competitive position	Strong
<b>Financial risk</b>	<b>Intermediate</b>
Cash flow/leverage	Intermediate
<b>Anchor</b>	<b>bbb+</b>
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Strong (no impact)
Management and governance	Positive (no impact)
Comparable rating analysis	Neutral (no impact)
<b>Stand-alone credit profile</b>	<b>bbb+</b>

## Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

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